89- 1500

No.

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1989

BUSINESS GUIDES, INC.,
Petitioner,

VS.

CHROMATIC COMMUNICATIONS ENTERPRISES, INC.
and MICHAEL SHIPP,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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QUESTION PRESENTED

Under Federal Rule of Civil Procedure 11, may a represented party be sanctioned for submitting erroneous information to the district court when it believed, in good faith, in the accuracy of such information based on an examination of its business records?

II

PARTIES

In addition to the parties named in the caption, pursuant to Rule 28.2 petitioner identifies the following parties which may have an interest in the outcome of the petition: Lebhar-Friedman, Inc. (parent of petitioner); Chain Store Publishing Corp. (corporate affiliate of Lebhar-Friedman, Inc.); and Largo Music, Inc. (corporate affiliate of Lebhar-Friedman, Inc.).

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Petitioner respectfully requests that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Ninth Circuit in this case.

OPINIONS BELOW

The February 16, 1990 decision of the United States District Court for the Northern District of California is reprinted at Pet. App. 1a-2a. The December 21, 1989 opinion of the United States Court of Appeals for the Ninth Circuit is reported at 892 F.2d 802 and is reprinted in the appendix to this petition at Pet. App. 3a-26a. The August 5, 1988 decision of the United States District Court for the Northern District of California is reported at 121 F.R.D. 402 and is reprinted at Pet. App. 27a-34a. The April 12, 1988 decision of the United States District Court for the Northern District of California is reported at 119 F.R.D. 685 and is

reprinted at Pet. App. 35a-46a. The September 14, 1987 Magistrate's revised report and recommendation is reprinted at Pet. App. 47a-63a. The April 3, 1987 Magistrate's report and recommendation is reprinted at Pet. App. 64a-81a.

JURISDICTION

The judgment of the Court of Appeals was entered on December 21, 1989. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

RULE INVOLVED

The Federal Rule of Civil Procedure involved herein is Rule 11, which provides in pertinent part:

> Every pleading, motion, and other paper of a party represented by an attorney shall be signed by at least one attorney of record in the attorney's individual name, whose address shall be stated. A party who is not represented by an attorney shall sign the party's pleading, motion, or other paper and state the party's address. . . . The signature of any attorney or party constitutes a certificate by the signer that the signer has read the pleading, motion, or other paper; that to the best of the signer's knowledge, information and belief formed after reasonable inquiry it is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law, and that it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation. If a pleading, motion, or other paper is signed in violation of this rule, the court, upon motion or upon its own initiative, shall impose upon the person who signed it, a represented party, or both, an appropriate sanction, which may include an order to pay to the other party or parties the amount of the reasonable expenses incurred because of the filing of the pleadings, motion, or other paper, including a reasonable attorney's fee.

(As amended Apr. 28, 1983, eff. Aug. 1, 1983).

STATEMENT OF THE CASE

A. Summary of the Legal Issue Presented

Petitioner Business Guides, Inc. was sanctioned by the district court under Rule 11 for submitting erroneous information in connection with its prosecution of an action for copyright infringement. Business Guides concededly made a mistake; it relied on the accuracy of a business record which, it subsequently became apparent, was inaccurate. But there also is no dispute that its mistake was an honest one; Business Guides had no intent to mislead the Court or submit erroneous evidence.[1] Nonetheless, the district court held, and the Ninth Circuit affirmed, that such good faith does not preclude a represented party from being sanctioned under Rule 11. Specifically, the court below held that the "objective" standard of reasonableness applicable to attorneys should be applied, as well, to represented parties. That holding frames the issue presented by this petition: namely, whether in light of the policies underlying Rule 11, a *party* may be sanctioned even though it indisputably has acted in good faith. As to that issue there is a direct conflict between the decision of the Ninth Circuit in this case and the decision of the Second Circuit in *Calloway v. Marvel Entertainment Group*, 854 F.2d 1452 (2d Cir.), *rev'd in part on other grounds sub nom. Pavelic & Leflore v. Marvel Entertainment Group*, ___ U.S. ___, 110 S. Ct. 456 (1989).

The issue bears consideration by this Court. Rule 11 has become one of the most important of the Federal Rules as the

[1] As explained more fully at pp. 10-12 *infra* the court (or to be precise, a Magistrate to whom the matter was referred) originally held to the contrary. The Magistrate initially found both Business Guides and its former counsel guilty of intentional deception. However, after Business Guides obtained new attorneys who were able to explain to the court what actually happened, the Magistrate expressly vacated his finding of bad faith. He nonetheless sanctioned Business Guides for having been careless in filing and prosecuting its suit for copyright infringment. It is that finding, affirmed both by the district court and, thereafter, by the Ninth Circuit, which forms the basis for the present petition.

increase in complex litigation and its unquestioned potential for abuse have led courts to scrutinize the conduct of such litigation with greater care. Rule 11 has become a critical mechanism for policing litigation abuse. At the same time, however, the very potential for sanctions under Rule 11 is, itself, capable of tactical misuse—a point which a number of courts and commentators have noted with apprehension. *See, e.g., Operating Engineers Pension Trust v. A-C Co.*, 859 F.2d 1336 (9th Cir. 1988); Snyder, *The Chill of Rule 11*, 11 Litigation (Winter 1985). Rule 11 sanctions have the potential to chill the assertion of legitimate claims as well as deterring misconduct. A line must carefully be drawn, therefore, which accomplishes the latter, but not the former.

That line, we submit, is the one drawn by the Second, not the Ninth, Circuit. The role of Rule 11 is different in regard to lawyers and their clients. As officers of the court, trained and licensed as to their professional competence, it is entirely appropriate to hold counsel to a baseline standard of (objective) competence in the prosecution or defense of litigation. Thus, it is perfectly appropriate to apply a standard of objective reasonableness to their conduct, as the cases under Rule 11 indisputably require. *E.g., Zaldivar v. City of Los Angeles*, 780 F.2d 823 (9th Cir. 1986); *Eastway Constr. Corp. v. City of New York*, 762 F.2d 243 (2d Cir. 1985), *cert. denied*, 484 U.S. 918 (1987).

The same is not true of parties who, in good faith, choose to bring litigation or who—in the course of such litigation—assert the existence or accuracy of certain facts, believing those assertions to be true, even though they are not. Certainly it is appropriate to sanction anyone who knowingly misuses the litigation process; but to sanction a party who believes—even if erroneously—that what he or she has said to the court is true crosses over the line which divides a legitimate concern for litigation abuse from excessive deterrence of potentially legitimate claims. Put otherwise, having an "empty head" in the case of a client should not offend the Federal Rules.[2]

[2] Nor, as we explain *infra* is there a need to employ Rule 11 to protect other parties as opposed to the litigation process. Those parties have the ability to seek relief through the common law torts of abuse of process and malicious prosecution. In fact, to the extent that the holding below purports to create a new "Rule 11" tort, or—even more plainly—establishes a basis for sanctions which extends beyond the common law principles governing abuse of process or malicious prosecution, a serious question is raised under the Rules Enabling Act, 28 U.S.C. § 2072, and the Constitution. *See, e.g., Sibbach v. Wilson & Co., Inc.*, 312 U.S. 655 (1941), *See also* pp. 21-22, *infra*.

There is good reason for granting the writ in this case even beyond the traditional ground that it involves a direct conflict between the circuits on a significant issue of law. In the past two terms this Court has agreed to review two cases raising important issues of attorney responsibility under Rule 11, *Pavelic & Leflore v. Marvel Entertainment Group*, ___ U.S. ___, 110 S. Ct. 456 (1989) and *Danik, Inc., v. Hartmarx Corp.*, 875 F.2d 890 (D.C. Cir.), *cert. granted sub nom. Cooter & Gell v. Hartmarx Corp.*, ___ U.S. ___, 110 S. Ct. (1989). Those cases test the limits of Rule 11 as, in a different way, does this one. While this Court must, of course, be the arbiter of its own docket, petitioner submits that, particularly in light of the conflict among the circuits, this case is a useful complement to *Pavelic & Leflore and Cooter & Gell* in defining the scope and limits of Rule 11 in an important respect.

B. Statement of Facts

Business Guides is a subsidiary of Lebhar-Friedman, Inc., a publisher of trade journals and magazines in the United States. Since 1983, Business Guides has published a directory of computer products and services. Since approximately 1985, respondent Chromatic Communications Enterprises, Inc. has published a similar directory. Both publications list the name, address and telephone numbers of computer store and software retailers in the United States, together with a brief description of each business.

Directories such as those published by Business Guides are laborious to compile, but relatively easy to copy. Thus, as a means of detecting copying by its competitors, Business Guides intentionally plants incorrect information, known as "seeds", in its directories. The use of such "seeds" is common among publishers

of directories and atlases. Business Guides uses two types of seeds. "Type A" seeds are entirely fictitious listings, *i.e.*, businesses which do not exist at all. "Type B" seeds, on the other hand, are partially altered listings which contain minor errors such as transposed numbers in an address or zip code or misspelled names. The appearance of one or more seeds in a competitor's publication is considered strong evidence of copyright infringement.

In the normal course of its business, Business Guides compiles and maintains "master seed lists" for each type of directory it publishes. These documents identify each of the Type A and B seeds which appear in particular directories. Normally, the seed list is prepared prior to publication and the seeds are intentionally inserted just before final printing. However, due to a concern that its 1984 computer directory did not contain enough seeds, Business Guides created its 1984 master seed list in a unique and—with hindsight—ill-advised fashion.

Specifically, Business Guides directed one of its employees, Victoria Burdick, to identify a new form of "after-the-fact" Type B seed; to wit, a list of unintentional typographical errors actually printed in the final version of the directory. To locate such errors, the employee compared the final 1984 directory against the initial information sheets (or questionnaires) used by Business Guides to gather information from the to-be-listed companies. When she found a disparity between the information listed in the questionnaires and the final directory, she recorded the discrepancy on the master list as a Type B seed. This approach, however, was unknowingly based on an incorrect premise. Ms. Burdick assumed that the erroneous information *on the questionnaires* was correct. In fact, the information on the questionnaires frequently had been revised by other Business Guides employees in the proofreading stage but without correcting the questionnaires themselves. Thus, the 1984 Master Seed List of purported errors actually contained numerous Type B seeds which were in fact *accurate*. The presence of similar listings in competitor's directories would therefore be consistent with independent research and would not establish any copyright infringement of Business Guide's directory.

The foregoing facts were, however, unknown to Business Guides at the time it filed the instant action. The findings of the magistrate and district court acknowledge that Business Guides did not understand the significance of the faulty preparation of the 1984 seed list until new counsel explained it to representatives of the company and thereafter to the court, long after the original lawsuit had been filed. Pet. App. 57a. Thus, however misdirected its efforts may ultimately have turned out to be, Business Guides did not know or suspect that this particular business record contained errors. It relied in good faith on its accuracy in commencing the underlying action.

Business Guides first suspected that Chromatic may have been copying its computer directory in 1985 due to the appearance of a so-called Type A seed from the 1984 master seed list in respondent's 1985 directory.[3] In 1986, respondent published a diskette version of its computer directory. That publication contained eight additional Type B seeds found on the 1984 master seed list, and one Type B seed from the 1985 master seed list.

Business Guides thereupon contacted its copyright counsel, the former law firm of Finley, Kumble, Wagner, Heine, Unterberg, Manley, Myerson & Casey ("Finley Kumble") and relayed to it the information regarding the appearance of ten "seeds" in respondent's directory. Finley Kumble did not request that Business Guides explain to it the specific inaccuracies in the ten listings which made them "seeds", nor did it suggest that Business Guides attempt to verify the information contained in the master seed lists or other business records. To the contrary, Finley Kumble advised petitioner that it had meritorious grounds to proceed with a lawsuit against respondent. Accordingly, Business Guides authorized, and Finley Kumble prepared and filed, a complaint for copyright infringement, conversion and unfair competition, together with an application for a temporary restraining

[3] That seed, "NFR Computer Room" was an entirely fictitious company, created from the initials of the daughter of one of Business Guides' employees (Nicole F. Rossini), the listed address actually was that employee's home address.

order seeking to prevent respondent from marketing its directory. That complaint was filed on October 31, 1986.

A hearing on the TRO was scheduled for November 7, 1986. Three days before the hearing, the district judge's law clerk telephoned Finley Kumble to request details regarding the incorrect information in each of the ten entries listed as "seeds".[4] Finley Kumble then contacted Michael Lambe, a mid-level manager who had not been involved in preparing the after-the-fact 1984 Master Seed List, and requested the additional information from him. This was the first time Finley Kumble asked for details about the ten seeds.

In an effort to respond to his counsel's inquiry, Mr. Lambe reviewed the 1984 Master Seed List and provided Finley Kumble with the requested details as they appeared on that document. In addition, ***entirely on his own initiative***, Mr. Lambe attempted to verify the information contained on the seed list by checking subsequent Business Guides publications and zip code directories. As a result of his inquires, Mr. Lambe had uncertainty about four of the seeds and he instructed Finley Kumble to withdraw them. Mr. Lambe verified three of the other seeds. He was unable to verify the remaining three seeds but testified that he felt no reason to doubt them. Mr. Lambe's continuing belief in the accuracy of the seed list was due in part to the fact that one of the remaining seeds was the Type A (wholly fictitious) NFR Computer Room seed which, to Mr. Lambe's knowledge and belief, could not have been included in defendants' publication in the absence of outright copying. His belief in the basic soundness of the "seeding" process was also supported by the fact that the company recently had relied on it to find copying by a subsidiary of Xerox which, when confronted with Business Guides' evidence, consented to an injunction.[5]

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[4] For reasons which remain inexplicable, Finley Kumble had not bothered to include that basic informatioin in the papers it prepared on behalf of its client.

[5] As discussed further, *infra*, both the magistrate and the district court found Mr. Lambe's reliance on the unchecked seeds unreasonable in view of the fact that his efforts had drawn other seeds into question. But even conceding that it may have been careless of him to so rely, the issue remains whether the purposes of Rule 11 are served by imposing sanctions against him (or, more precisely, his employer) in such circumstances. He was not trying to mislead anyone. In fact, the record is not disputed that he only discovered the errors he did locate because he had decided on his own initiative to check information in the original court papers.

Finley Kumble took the information provided by Mr. Lambe and put it into the form of a supplemental declaration which it submitted to Mr. Lambe for his review. That declaration was not given to Mr. Lambe until the morning of the November 7 TRO hearing, at which point he was told that it was urgent that he sign and return the document immediately. Mr. Lambe thus had only one or two hours to review the declaration drafted by counsel. He not only reviewed, but modified the declaration further.[6] He then signed it, believing in good faith in its accuracy. However (as proved dispositive in the opinion of the district and circuit courts), Mr. Lambe did not personally telephone the listed businesses to verify the remaining seeds listed in his supplemental declaration.

The district court's law clerk, on his own initiative, did just that. Due in part to the fact that the record had been sealed and to apparent uncertainty on his part as to whether Chromatics' attorney would have an opportunity to respond to the sealed TRO papers, the law clerk telephoned the companies listed in the remaining six seeds. In so doing, he concluded that five additional seeds actually contained correct information. As a result of this independent discovery, the district court refused oral argument, denied the TRO application, stayed all proceedings (including discovery) and referred the matter to a magistrate for a determination as to whether Finley Kumble and/or Business Guides should be sanctioned under Rule 11.

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[6] Of the four seeds Mr. Lambe questioned and asked to have withdrawn, Finley Kumble still included one in the declaration drafted for his signature. Mr. Lambe, concerned with not misleading anyone, refused to sign it without a further deletion. Thus, the declaration, as signed, actually showed one of the seeds crossed out in ink. *See* CR 54:9-10.

The magistrate conducted three separate evidentiary hearings on the Rule 11 issue. At the first two, and despite a seemingly obvious conflict, both Finley Kumble and Business Guides were represented by the same counsel, who contended that the factual errors contained in Mr. Lambe's supplemental declaration were merely coincidental. Following those two hearings, on April 3, 1987, the magistrate issued a report recommending that both Business Guides and Finley Kumble be sanctioned under Rule 11 and that a partner in the law firm be subject to further disciplinary proceedings. In his report, the magistrate stated that he doubted the good faith of the parties' representations, since he found it incredible that the factual errors in the Lambe declaration could be attributed to mere coincidence.

Business Guides then retained its present counsel, who undertook an entirely new investigation, as a result of which Business Guides filed objections to the magistrate's report. For the first time new counsel for Business Guides brought to the court's attention the fact that all of the problems in the evidence could be traced to the faulty methodology used (unbeknownst to Mr. Lambe) in preparing the 1984 Master Seed List. Based on this new evidence the Magistrate granted the application for a new hearing and on June 9, 1987, conducted a third evidentiary hearing at which the full story was finally presented. The magistrate then issued a revised report and recommendation in which he stated that he no longer believed that Business Guides or its counsel took part in any intentional misrepresentation or cover-up. *Business Guides v. Chromatic Communications Enterprises, Inc.*, 119 F.R.D. 685, 687 (N.D. Cal. 1988). Pet. App. 40a. The magistrate also found that Business Guide's lawsuit was not "interposed for any improper purpose." Pet. App. 53a.

Despite his revised finding that Business Guides had acted in good faith, the magistrate nonetheless recommended that Business Guides be sanctioned on three separate grounds: first, for filing the underlying lawsuit based on the inaccurate 1984 master seed list; second, for submitting Mr. Lambe's supplemental declaration without a "telephone check" of the information contained in the seed list; and third, for presenting the "coincidence" argument to the magistrate at the first two evidentiary hearings.

The district court adopted the magistrate's findings and recommendations, unsealed the record and invited respondent to seek specific monetary and other sanctions. *Business Guides v. Chromatic Communications Enterprises, Inc.*, 121 F.R.D. 402 (N.D. Cal. 1988). Pet. App. 27a-34a. After briefing by both sides (but without permitting oral argument) the district court imposed sanctions against Business Guides in the amount of $13,865.66 and dismissed its entire lawsuit (prior to any discovery) with prejudice.[7]

In its decision dated December 21, 1989, the Ninth Circuit affirmed in part, reversed in part, and vacated in part the district court's decision and remanded the case for further proceedings. The Ninth Circuit held that Rule 11 applies only to signed pleadings or other papers and thus could not apply to the arguments presented to the magistrate at the first two evidentiary hearings. However, the Court affirmed the imposition of sanctions against Business Guides for failing to conduct an objectively reasonable prefiling inquiry about the accuracy of the 1984 Master Seed List as well as for the errors contained in Mr. Lambe's supplemental declaration.

In rendering its decision, the Ninth Circuit expressly rejected petitioner's reliance on the leading case of *Calloway v. Marvel Entertainment Group*, 854 F.2d 1452 (2d Cir.), *rev'd in part on other grounds sub nom, Pavelic & Leflore v. Marvel Entertainment Group*, ___ U.S. ___, 110 S. Ct. 456 (1989), in which the Second Circuit held that while an objective standard of reasonable inquiry applies to the conduct of *attorneys* under Rule 11, a subjective (*i.e.* "good faith") standard of reasonableness applies to *represented parties*.

In rejecting the Second Circuit's standard, the Ninth Circuit stated that whether the objective or subjective standard applies to parties is "purely a legal matter" and was a matter of "first

[7] By this time, Finley Kumble had filed for bankruptcy, and respondent had withdrawn that part of its Rule 11 motion seeking sanctions from the law firm. Accordingly, neither the district court nor the court of appeals decided whether sanctions were appropriate as against Finley Kumble.

impression" in the Ninth Circuit. *Business Guides v. Chromatic Communications Enterprises, Inc.*, 892 F.2d 802, 808 (9th Cir. 1989). Pet. App. 13a, 15a. Based in large part on policy arguments and its reading of the Advisory Committee Notes to Rule 11, the Ninth Circuit held that "an objective standard applies to lawyers and represented parties alike." *Id.* at 812. Pet. App. 21a. The Court then affirmed the district court's determination that Business Guides failed to conduct an objectively reasonable inquiry before filing (1) the original complaint and (2) Mr. Lambe's supplemental declaration.[8]

REASONS FOR GRANTING THE PETITION

Since its amendment in 1983, practice under Rule 11 has become a cottage industry of the litigation bar. In 1988, Judge William W. Schwarzer of the Northern District of California estimated that over six hundred decisions enforcing or interpreting Rule 11 had been reported in the five years since the 1983 amendment. Schwarzer, *Rule 11 Revisited*, 101 Harv. L. Rev. 1013 (1988). Unfortunately, the rule has been not only vigorously, but unevenly, applied. *See Eastway Constr. Corp. v. City of New York*, 821 F.2d 121 (2d Cir. 1987) (Pratt, J. dissenting) ("apparent disparities, even capriciousness, [now seem] to characterize much of Rule 11 jurisprudence"), *cert. denied*, ___ U.S. ___, 108 S. Ct. 269 (1987).

A survey conducted by the Federal Judicial Center (FJC) illustrates these substantial inconsistencies in the application of Rule 11. The survey was based on ten hypothetical cases adapted

[8] In light of the fact that the Court of Appeals reversed the imposition of sanctions on one ground (but affirmed on two others), it vacated the order of sanctions and remanded the case to the district court to reconsider its choice of sanctions. Without permitting briefs or holding oral argument, the district court on February 16, 1990, issued an order *sua sponte* dismissing the underlying action and, seeing no need for modification, reaffirming the imposition of the original $13,865.66 in monetary sanctions. P[illegible] App. 1a. This petition thus pertains to a final judgment and involves a legal issue conclusively passed upon by the Court of Appeals.

from real cases involving Rule 11 motions. When asked to assess whether a Rule 11 violation had occurred, the 292 participating federal judges responded to individual cases very differently. The proper application of Rule 11 was so unclear that almost half the judges in the survey would have sanctioned the same paper that the other half of the responding judges thought did not violate the rule. One explanation the FJC report offered for this lack of consensus was disagreement over how to interpret Rule 11's generalized standards. Note, *Plausible Pleadings: Developing Standards for Rule 11 Sanctions*, 100 Harv. L. Rev. 630, 641 (1987) (citing S. Kassin, *An Empirical Study of Rule 11 Sanctions* 38 (Federal Judicial Center 1985)).

Thus, one commentator has stated:

> [I]t is apparent that not all judges agree, in philosophy or in practice, on precisely what conduct constitutes a violation of the rule. Practicing under Rule 11 is like negotiating a minefield. You know there will be an explosion if you step on a mine. The trouble is, you don't know where the mines are.

Joseph, *The Trouble with Rule 11—Uncertain Standards and Mandatory Sanctions*, 73:8 A.B.A.J. 87, 88-9 (1987). *See also*, Schwarzer at 1015 ("in interpreting and applying Rule 11, the courts have become a veritable Tower of Babel"); Note, 100 Harv. L. Rev. at 650 ("Erratic application of Rule 11 threatens to convert it from a constructive principle for case load management into a random instrument of judicial intimidation. . . . A scattershot rule . . . deters too much; it is unnecessarily costly in terms of chilling valid litigation.")

This Court recently has considered two Rule 11 cases involving the responsibility of *attorneys* under Rule 11. *Pavelic & Leflore v. Marvel Entertainment Group*, ___ U.S. ___, 110 S. Ct. 456 (1989) and *Danik, Inc. v. Hartmarx Corp.*, 875 F.2d 890 (D.C. Cir.), *cert. granted Sub nom. Cooter & Gell v. Hartmarx Corp.*, ___ U.S. ___, 110 S. Ct. 275 (1989). In *Pavelic*, the Court held that the individual attorney signing a pleading is subject to Rule 11 sanctions, but not his law firm. In *Cooter & Gell*, the Court apparently has agreed to decide whether jurisdiction exists to impose Rule 11 sanctions following a plaintiff's voluntary dismis-

sal pursuant to Fed R. Civ. P. 41, and whether sanctions on appeal *automatically* should be imposed upon affirmance of a Rule 11 award. These decisions, while certainly important, do not provide any guidance as to the legal standard for imposing sanctions on *parties* under Rule 11.[9] The two circuits which have addressed that issue—the Ninth and the Second—have come to entirely different conclusions.

Under the standard applied in the Second Circuit, so long as a represented party acts in good faith and truthfully presents the facts as it believes them to be to counsel, the party may not be sanctioned under Rule 11. *Calloway,* 854 F.2d at 1474-5: *Greenberg v. Hilton Int'l. Co.*, 870 F.2d 926 (2d Cir. 1989). By contrast the Ninth Circuit in this case held that represented parties must conduct an "objectively reasonable" prefiling investigation before authorizing counsel to initiate an action.[10]

It is by now well-settled that in the case of counsel, the applicable standard under Rule 11 is one of objective reasonableness. As colorfully put by Judge Schwarzer. "[T]here is no room for a pure heart, empty head defense under Rule 11." Schwarzer, *Sanctions Under The New Federal Rule 11 - A Closer Look*, 104

[9] In fact, in both cases where this Court granted *certiorari,* the represented party (along with counsel) had also been sanctioned under Rule 11. However, in *Calloway,* the represented party failed to prosecute his appeal. Thus, one of the most important holdings of that case—that the subjective standard of reasonableness applies to represented parties —was not reviewed by this Court. In *Cooter & Gell*, the represented party declared bankruptcy and therefore did not prosecute its appeal. Here, conversely, Finley Kumble has been effectively immunized from the proceedings through bankruptcy, and it is the represented party that seeks the guidance of this Court.

[10] In its opinion below, the Ninth Circuit claims support for its holding from the Fourth Circuit's opinion in *Cleveland Demolition Co. v. Azcon Scrap Corp.*, 827 F.2d 984 (4th Cir. 1987). However, that opinion did not discuss the responsibilities of *represented parties* under Rule 11. To the contrary, the *Cleveland Demolition* court stated: "To fulfill his duty, an *attorney* must investigate the facts, examine the law, and then decide whether the complaint is justified." *Id.* at 988 (emphasis added).

F.R.D. 181, 187 (1985). In fact, the Second Circuit was one of the first courts to recognize that, under amended Rule 11, "subjective good faith no longer provides the safe harbor it once did" for attorneys. *Eastway Constr. Corp. v. City of New York*, 762 F.2d 243, 253 (2d Cir. 1985), *cert. denied.*, 484 U.S. 918 (1987). In the case of represented parties, however, the same court has concluded that subjective good faith precludes the imposition of Rule 11 sanctions: "[A]n 'objectively reasonable test' . . . is appropriate only in evaluating the conduct of attorneys under Rule 11, not the conduct of parties represented by attorneys." *Calloway,* 854 F.2d at 1474. As explained by the Second Circuit:

> As licensed professionals and officers of the court, attorneys are expected to measure up to minimal standards of professional competence under the Rule and thus may not excuse their conduct on the ground that they were acting in good faith. . . .
>
> We believe that a party represented by an attorney should not be sanctioned for papers signed by the attorney unless the party had actual knowledge that filing the paper constituted wrongful conduct, *e.g.*, the paper made false statements or was filed for an improper purpose. . . .
>
> We believe that where a represented party either did not knowingly authorize or participate in the filing of a paper that violated Rule 11, sanctions against that party are not appropriate. We further believe that when a party has participated in the filing of a paper signed by the attorney or has signed a paper himself but did not realize that such participation or signing was wrongful, then sanctions against the party are also not appropriate. . . .
>
> *Id.* at 1474-5.

Calloway has been followed consistently within the Second Circuit. *See, e.g.*, *Greenberg*, 870 F.2d at 934 ("Where a party represented by an attorney is the target of a Rule 11 motion . . . the subjective good faith test applies.") *See also Quadrozzi v. City of New York*, 127 F.R.D. 63 (S.D.N.Y. 1989); *Alberts v. Wall Street Clearing Corp.*, 1989 U.S. Dist. LEXIS 7945, at 6 n.1

(S.D.N.Y. July 13, 1989). Under the Second Circuit's test, petitioner would not have been sanctioned under Rule 11. As the district court expressly found, neither Business Guides nor its employee, Mr. Lambe, intended to mislead the court, Pet. App. 53a; nor did Business Guides even understand the significance of the faulty preparation of the 1984 master seed list until four years after that document was prepared. Pet. App. 57a.

The Ninth Circuit acknowledged but expressly rejected the Second Circuit's test. Instead, the Ninth Circuit held that the proper test for both attorneys and their clients is "objective reasonableness under the circumstances." The distinction, if any, according to the Ninth Circuit lies not in the applicable standard but in its application: "What is objectively reasonable for a client," said the court, "may differ from what is objectively reasonable for an attorney." *Business Guides*, 892 F. 2d at 810. Pet. App. 18a. Applying this standard, the court held that an objectively reasonable litigant under the circumstances would have conducted a telephone check, as did the district court's law clerk. *Id.* at 812. Pet. App. 22a.

By its holding, the Ninth Circuit not only rejected the Second Circuit's "good faith" test but, petitioners submit, created a standard which is needlessly harsh and amorphous. It is a standard destined to confound district courts and chill legitimate claims, contrary to the express caution of the Rules Advisory Committee. *See* Fed. Rule. Civ. P. 11 Advisory Committee Note to 1983 Amendment, 97 F.R.D. 198, 199 (1983).

There are several significant problems with the Ninth Circuit's approach. *First*, the function of Rule 11 is—or, we submit, should be—different in the case of parties and their counsel. As officers of the court there is reason to be concerned with attorneys' competence, diligence and integrity in the performance of their professional tasks. Whether or not counsel acts in good faith, therefore, it is a matter of legitimate judicial concern if his or her conduct falls below baseline standards.[11]

[11] *See*, Note, *The Demise of a Subjective Bad Faith Standard Under Amended Rule 11*, 59 Temp. L.Q. 107, 137 (1986) ("objective standard of reasonable inquiry . . . accommodates the attorney's role as advocate

The same concern is not appropriate for parties. So long as such parties act in good faith, tell the whole truth and nothing but, they should be entitled to rely on the advice of counsel as to whether they need to verify certain facts or business records, or take other steps before filing suit.[12]

Second, the Ninth Circuit test—which directs courts to apply the same standard of "objective reasonableness" but, then, to analyze what *is* reasonable differently for counsel and parties—is not only hopelessly vague but will create myriad problems in application. Thus, it will not only exacerbate the already serious problem of non-uniformity under Rule 11 but will promote extended and costly factual inquiries in each Rule 11 proceeding.

with the attorney's ethical duty as an officer of the court."); *see also Lepucki v. Van Wormer*, 765 F.26 86, 87 (7th Cir.), *cert. denied sub nom. Hyde v. Van Wormer*, 474 U.S. 827 (1985) (as officers of the court attorneys have an ethical and legal obligation to carefully review claims for truthfulness and sufficiency prior to submitting them); *Mohammed v. Union Carbide Corp.*, 606 F. Supp. 252, 261 (E.D. Mich. 1985) (in representing client, attorney cannot avoid duty owed to the administration of justice). *See generally* Model Code of Professional Responsibility DR 7-102(A) (1982) and Model Rules of Professional Conduct, Rules 3.1 & 3.3 (1983).

[12] The Ninth Circuit also believes that the objective standard of reasonableness applies to *pro se* parties. *See*, *Business Guides*, 892 F.2d at 811, Pet. App. 20a.; *Zaldivar v. City of Los Angeles*, 780 F.2d 823 (9th Cir. 1986); Advisory Committee Note, 97 F.R.D. at 199 ("the [reasonable inquiry] standard is the same for unrepresented parties.") However, this view is informed by the notion that when parties represent themselves they also must act, in some senses, as officers of the court. Without counsel to ensure that the federal rules, among others, are complied with, *pro se* parties must undertake that obligation and be held accountable for failure to fulfill it. *Moon v. Newsome*, 863 F.2d 835 (11th Cir.), *cert. denied*, 110 S. Ct. 180 (1989); *Royce Int'l Broadcasting Co. v. F.C.C.*, 820 F.2d 1332 (D.C. Cir. 1987); *Kelley v. Secretary of Labor*, 812 F.2d 1378 (Fed. Cir. 1987). Our system of justice thus encourages litigants to retain counsel. *See, e.g., Spainhower v. United States*, 469 U.S. 1193 (1985). (Sixth Amendment not violated when court appointed standby trial counsel for *pro se* defendant). Application of the subjective test to represented parties will further encourage litigants to utilize retained or court-appointed attorneys, and to rely on such attorneys to ensure adequate prefiling factual and legal inquiry.

Presumably, the Ninth Circuit's "objective reasonableness" test would vary from the case of a plaintiff with a second grade education, to the naturalized citizen unfamiliar with the American legal system to the sophisticated businessman and frequent litigant. And what will be the standard for litigants like the plaintiff in *Calloway* who, the record indicates, may have been "mentally ill"? *Calloway*, 854 F.2d at 1465. In addition to the characteristics of the represented party, other variables in the "reasonable litigant" test presumably would include the complexity of the subject litigation and the nature of the litigant's business. The determination of "objective reasonableness under the circumstances", in short, will require just the type of extensive "satellite" Rule 11 proceedings which courts have been admonished to avoid. *See* Advisory Committee Note, 97 F.R.D. at 201.

The Ninth Circuit understandably did not attempt to provide guidance as to what constitutes "reasonable" behavior for represented parties. In the case of attorneys, objectively reasonable behavior at least is defined uniformly—if not very precisely—as adherence to "minimal standards of professional competence." *Calloway*, 854 F.2d at 1474. But is there such a minimum level of competence for all parties from all walks of life, with all levels of education and experience, who find themselves (voluntarily or involuntarily) parties in federal court litigation? If so, the decision below is silent as to such standards, and represented parties can only guess as to whether their actions will be judged "reasonable." *Cf., Note, A Uniform Approach To Rule 11 Sanctions*, 97 Yale L.J., 901, 902 (1988) (Nonuniform Rule 11 decisions "have created an impression of arbitrariness . . . .")[13]

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[13] "Fairness requires the legal system to apply uniform standards to those who are similarly situated. Guidelines that address whom to sanction and factors to be weighed in determining appropriate sanctions are especially needed to ensure equal treatment under Rule 11, since a major argument undercutting the Rule's legitimacy has been that disagreement among judges has produced widely disparate results. Moreover, such guidelines would provide better notice to lawyers and clients about their respective areas of responsibility for frivolous submissions, and increase judicial efficiency in administering Rule 11 cases."

Note, 97 Yale L.J. at 913.

Third, there simply is no need to test the conduct of a party by the same standard (or even more or less the same standard, see above) as is applied to counsel. It is a reasonable goal to prevent a party from abusing the courts by filing litigation which it knows is baseless but files for the purpose of harassment or some other vexatious purpose. Similarly, there is never justification for knowingly submitting false evidence. But there is no need to go further and punish a client who believes in good faith that what she has told her attorney is accurate, even if it turns out not to be on account of some unknown fact. That is true even if, as lawyers or judges, we might find the party's failure to check further to be negligent. The right to seek redress of grievances is simply too important to erect barriers which will overly deter the assertion of potentially valid claims because of a fear that some mistaken fact or assumption later will be discovered and that the failure to appreciate it thereafter will be held "unreasonable". If there is to be a "screen" for such errors it is far better to place it upon counsel who are charged with knowing the types of questions to ask and the pre-filing inquiries to pursue.

To the extent there is any legitimate concern with the conduct of parties beyond the filing of litigation known to be baseless or with the making of knowingly false statements, it is that litigation may be filed with total indifference to its truth or merit. But that is simply an issue of what to do about so-called "recklessness," or "reckless indifference," which is a subject that this Court has confronted and dealt adequately with elsewhere. For example, in cases involving alleged defamation of public figures or officials, this Court has limited actions to those which are brought with "actual malice," *i.e.*, subjectively in bad faith. *E.g., New York Times v. Sullivan*, 376 U.S. 254 (1964). However, to avoid the problem of indifference, the Court has defined malice to include both knowing misstatements and statements made with "reckless disregard" of their accuracy. *Id.* at 280. Similarly, the finding of "scienter" required under Rule 10b-5 can encompass either knowing or *reckless* misrepresentations or omissions. *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975). See also, *Hackbart v. Holmes*, 675 F.2d 1114 (10th Cir. 1982); *Sharp v.*

Cooper & Lybrand, 649 F.2d 175 (3rd Cir. 1981), *cert. denied*, 455 U.S. 938 (1982). Given these holdings in areas of far more substantive significance, Rule 11 surely asks enough of lay people if it assures that they do not intend to deceive and are not recklessly indifferent about whether they have done so. To go beyond that and impose an objective standard of competence on them serves no readily cognizable policy of judicial management under Rule 11[14].

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[14] The Ninth Circuit's opinion also seemingly conflicts with the views of the Advisory Committee on the Federal Rules of Civil Procedure. In its comments to the 1983 amendments the Committee noted that

> "Even though it is the attorney whose signature violates the rule, it may be appropriate under the circumstances of the case to impose a sanction on the client. *See Browning Debenture Holders' Committee v. DASA Corp.* [560 F.2d 1078 (2d Cir. 1977)]"

Advisory Committee Note, 97 F.R.D. at 200.

The Committee's citation to *Browning* indicates that, in the case of represented parties, a good faith standard was intended to apply. In *Browning*, certain debenture holders appealed from an unfavorable judgment in a securities fraud and breach of fiduciary duty case against the defendant debenture trustee, and the trustee sought attorney's fees. The *Browning* court refused to impose fees against plaintiffs personally unless it could be demonstrated "*that they personally were aware of or otherwise responsible for the procedural action instituted in bad faith.*" *Browning*, 560 F.2d at 1089 (emphasis added).

The Second Circuit has interepreted the Committee's reference to *Browning* in precisely this fashion:

> "We believe that a party represented by an attorney should not be sanctioned for papers signed by the attorney unless the party had actual knowledge that filing the paper constituted wrongful conduct, *e.g.*, the paper made false statements or was filed for an improper purpose. The Advisory Committee stated that allocation of sanctions among attorneys and their clients was a matter of judicial "discretion" and that sanctions should be imposed on a party where appropriate under the circumstances. Fed. R. Civ. P. 11 Advisory Committee's Note to 1983 amendment. As guidance, the committee cited *Browning Debenture Holders Committee v. DASA Corp.*, 560 F.2d 1078 (2d Cir. 1977), a case holding that a represented party should not be held liable for wrongful conduct by attorneys unless the party was personally aware of or responsible for the conduct."

Calloway, 854 F.2d at 1471.

In the decision below, the Ninth Circuit attempted to distinguish *Browning* by noting that it was an "improper purpose" (rather than a Rule 11 inquiry) case. *Business Guides*, 892 F.2d 802, 811. Pet. App. 19a. But that is precisely the point. The Advisory Committee's reference to *Browning* indicates that for represented parties, sanctions under Rule 11 should be limited to conduct which otherwise would justify the imposition of attorney's fees—actions taken in bad faith or for an improper purpose.

Fourth, to punish a party for what "it should have known," as the Ninth Circuit suggests, 892 F.2d at 811, Pet. App. 20a, effectively extends state abuse of process and malicious prosecution jurisprudence in the context of interpreting a federal rule of civil procedure. Those common law torts seek on the one hand to prevent wasteful litigation while recognizing the right of represented parties, under most circumstances, simply to be wrong. Thus, in most jurisdictions, for example, "malice" (*i.e.* bad faith or recklessness) and lack of probable cause are requisite elements of a claim for malicious prosecution. *See, e.g., Dellums v. Powell*, 566 F.2d 167 (D.C. Cir. 1977), *cert. denied*, 438 U.S. 916 (1978) (private individuals immunized from tort liability for malicious prosecution so long as they do not act with malice, even if they act unreasonably); *Howell v. Davis*, 374 N.E.2d 393 (1978) (applying New York law); *Citizens State Bank v. Hoffman*, 44 Cal. App. 2d 854 (1941) (under California law, proof of reliance on the advice of counsel in good faith after truthful disclosure of the facts usually establishes probable cause.)

In fact, to rewrite such state tort laws under the guise of interpreting a federal rule of civil procedure would raise serious concerns under both the Rules Enabling Act, 28 U.S.C. § 2072, and the Constitution. *See Sibbach v. Wilson & Co. Inc.*, 312 U.S. 655 (1941); *Erie R.R. v. Tompkins*, 304 U.S. 64 (1938). The federal rules may not confer substantive rights upon parties inconsistent with applicable state law,[15] nor may they "abridge,

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[15] *See, e.g., Synanon Church v. United States*, 557 F. Supp. 1329 (D.D.C. 1983), *aff'd*, 820 F.2d 421 (D.C. Cir. 1987); *Haas v. Pittsburg*

enlarge or modify' any such substantive law. 28 U.S.C. § 2072. That Rule 11 (as interpreted by the Ninth Circuit) is "outcome determinative' and therefore violative of the *Erie* test, (*see Hanna v. Plumer*, 380 U.S. 460 (1965)), is underscored by the fact that Business Guide's claims in this case were dismissed with prejudice. There is no doubt that Congress has a legitimate interest in permitting courts to establish rules that assure the integrity of the litigation process, such as by enforcing minimal standards for counsel or preventing the submission of knowingly false evidence. However, a rule which effectively creates a federal tort of malicious prosecution without even its standards or prerequisites is more than an "incidental" infringement. *Id.* at 464-65. At a minimum, this question provides still further grounds for granting review.

CONCLUSION

One of Congress' primary purposes in authorizing a single set of federal rules was to ensure a "uniform and consistent system of rules governing federal practice and procedure. . . ." *Burlington N. R.R. Co.*, 480 U.S. at 5. It is for that reason, presumably, that this Court frequently has exercised its discretionary authority of review to assure consistent application of those rules.[16] Here that

Nat'l. Bank, 60 F.R.D. 604 (D. Pa. 1973). *Cf. Burlington N. R.R. Co. v. Woods*, 480 U.S. 1 (1986) (Rule 38 of the Federal Rules of Appellate Procedure, providing for discretionary damages for frivolous appeals, supersedes (in diversity actions) Alabama's mandatory 10% penalty statute).

[16] *See, e.g.,* See *Schiavone v. Fortune*, 477 U.S. 21 (1986) (certiorari granted because of an apparent conflict among the Courts of Appeals regarding Fed. R. Civ. P. 15(c); *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242 (1986) (certiorari granted to resolve conflict concerning standard to be applied under Fed. R. Civ. P. 56); *Daily Income Fund, Inc. v. Fox*, 464 U.S. 523 (1984) (certiorari granted to resolve a conflict regarding demand requirement of Fed. R. Civ. P. 23.1); *White v. N.H. Dept. of Employment Security*, 455 U.S. 445 (1982) (certiorari granted to resolve the timeliness standard set forth in Fed. R. Civ. P 56(e)); *Snyder v. Harris*, 394 U.S. 332 (1969) (certiorari granted to resolve the conflict of whether Rule 23 allows separate claims to be aggregated to

uniformity is threatened both by the conflict between the Second and the Ninth Circuits and by the needlessly open-textured standard adopted by the court of appeals in this case. We respectfully submit that practice under Rule 11 has become extremely important to the processes of litigation in the federal courts and that the issue of what standard of conduct should be applied to parties under that Rule is a matter of substantial importance to the proper administration of justice. For those reasons, it is appropriate for this court to review the decision below and resolve the conflict among the Circuits.

Accordingly, and for the foregoing reasons, Business Guides respectfully requests that its petition for a writ of certiorari be granted.

Respectfully submitted,

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meet the $10,000 jurisdictional minimum); *State Farm Fire & Casualty Co. v. Tashire*, 386 U.S. 523 (1967) (certiorari granted because the case involved "a matter of significance to the administration of federal interpleader").

APPENDIX

No. C 86 6164 SC

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

BUSINESS GUIDES, INC.,
Plaintiff,
v.
CHROMATIC COMMUNICATIONS
ENTERPRISES, INC., et. al.,
Defendants.

ORDER RE RULE 11

SANCTION OF DISMISSAL

In *Business Guides v. Chromatic Communications, Inc.*, 119 F.R.D. 685, 687-88 (D.C. Cal. 1988), this court ruled that Business Guides Inc. ("Business Guides") violated Rule 11 of the Federal Rules of Civil Procedure. The court found that Business Guides acted unreasonably in (1) filing a TRO application based on inaccurate facts; (2) failing to conduct a reasonable factual inquiry after being put on notice of inaccuracies in the TRO application; and (3) making "wholly unsupportable" oral representations to a magistrate at the sanctions proceedings.

Subsequently, in *Business Guides v. Chromatic Communications Enterprises ("Business Guides II")*, 121 F.R.D. 402 (N.D. Cal. 1988), this court awarded $13,865.66 to Chromatic Communications Enterprises, Inc. ("Chromatic") for Chromatic's legal expenses incurred in defending against the frivolous TRO action and in bringing the motion for sanctions. The court also ordered dismissal with prejudice of Business Guides' action because of "the rather remarkable circumstances of this case." *Id* at 406.

On appeal, the Ninth Circuit affirmed the court's imposition of sanctions for Business Guides' TRO application and subsequent failure to make a reasonable factual inquiry but reversed with respect to the oral representations because "Rule 11 does not apply to oral arguments or testimony before the court." *Business Guides, Inc. v. Chromatic Communications Enterprises, Inc.*, No. 88-15240, slip op., 14643, 14667 (9th Cir. 1989). The court

vacated the dismissal sanction and remanded it for reconsideration because it did not know if this court would "consider a sanction of dismissal appropriate in view of Business Guides' two rather than three violations." *Id* at 14668.

Upon reconsideration, the court sees no reason to lift its imposition of the dismissal sanction against Business Guides. The fact that Business Guides' lawyers' oral representations are not properly sanctionable under Rule 11 does not at all change the "rather remarkable circumstances" of this case. The filing of the TRO and the failure to make a reasonable factual investigation were and are sufficient grounds for the imposition of the sanction of dismissal. *See Business Guides II*, at 406.

In accordance with the foregoing, it is hereby ORDERED that Business Guides' action be dismissed with prejudice pursuant with this court's award of sanctions under Rule 11.

IT IS SO ORDERED.

Dated: February 16, 1990.

United States District Judge

BUSINESS GUIDES, INC.,
Plaintiff-Appellant,

v.

CHROMATIC COMMUNICATIONS
ENTERPRISES, INC.; MICHAEL SHIPP,
Defendants-Appellees.

No. 88-15240.

United States Court of Appeals,
Ninth Circuit.

Argued and Submitted June 28, 1989.

Decided Dec. 21, 1989.

Publisher of business directory brought action against competitor for copyright infringement, conversion, and unfair competition. The United States District Court for the Northern District of California, 121 F.R.D. 402, Samuel Conti, J., imposed sanction against publisher which included payment of competitor's legal expenses and dismissal of publisher's action. Publisher appealed. The Court of Appeals, Wallace, Circuit Judge, held that: (1) objective standard of reasonable inquiry into factual basis of papers submitted to court was appropriate standard to apply when determining whether sanctions should be imposed against represented party; (2) sanctions were appropriately imposed against publisher for failing to verify false information or "seeds" placed in its directory before filing papers and requesting temporary restraining order against competitor; (3) oral representations and testimony made to magistrate were not sanctionable; and (4) competitor's successful defense on appeal of imposition of sanctions against publisher did not automatically entitle competitor to award of attorneys' fees.

Affirmed in part, reversed in part, vacated in part, and remanded.

1. Copyrights and Intellectual Property 83(4)

Appearance in competitor's directory of one or more "seeds," such as wholly fictitious entries or partially altered listings which have been purposefully placed in another publisher's copyrighted directory, is strong evidence that copyrighted material has been appropriated by competitor.

2. Federal Civil Procedure —2721

Objective standard of reasonable inquiry into factual basis of papers submitted to court is appropriate standard to apply when determining whether sanctions should be imposed on represented parties. Fed.Rules Civ.Proc.Rule 11, 28 U.S.C.A.

3. Federal Civil Procedure —2721

For purpose of awarding sanctions, "reasonable" inquiry which attorney must make into factual basis for paper submitted to court is not the same as "reasonable" inquiry which client must make into factual basis. Fed.Rules Civ.Proc.Rule 11, 28 U.S.C.A.

4. Federal Civil Procedure —2721

Failure of publisher of business directory to take any steps whatsoever to verify false information or "seeds" in directory before filing court papers and requesting temporary restraining order against competitor, which allegedly published business directory containing "seeds," was objectively unreasonable, and thus sanctionable. Fed.Rules Civ.Proc.Rule 11, 28 U.S.C.A.

5. Federal Civil Procedure —2721

Failure of business directory publisher's research director to conduct more thorough investigation of false information or "seeds" placed in its directory, upon discovering that three or four out of ten "seeds" were baseless, was objectively unreasonable, and thus director's submission of affidavit referring to competitor's directory's use of "seeds" in proceeding requesting temporary restraining order against competitor was sanctionable. Fed.Rules Civ.Proc.Rule 11, 28 U.S.C.A.

6. Federal Civil Procedure —2721

Rule of Civil Procedure did not permit sanctions to be imposed on party for oral representations and testimony made to magistrate, as rule applies only to "pleading, motion, or other paper." Fed.Rules Civ.Proc.Rule 11, 28 U.S.C.A.

7. Federal Civil Procedure —2743

Party which successfully defended on appeal the imposition of sanctions on opposing party was not automatically entitled under Rule of Civil Procedure on sanctions to award of attorneys' fees on appeal, as legal costs on appeal were not costs "incurred because of" the filing in district court, within meaning of Rule. Fed.Rules Civ.Proc.Rule 11, 28 U.S.C.A.

Stephen V. Bomse, San Francisco, Cal. for plaintiff-appellant.

Neil L. Shapiro, Cooper, White & Cooper, San Francisco, Cal., for defendants-appellees.

Appeal from the United States District Court for the Northern District of California.

Before WALLACE, POOLE and HALL, Circuit Judges.

WALLACE, Circuit Judge:

Business Guides, Inc. (Business Guides) appeals from an order imposing Rule 11 sanctions in its copyright action against Chromatic Communications Enterprises, Inc. (Chromatic) and Shipp, Chromatic's president. Business Guides argues that the district court (1) erred in applying to Business Guides, a represented party, an *objective* standard of "reasonable inquiry" into the factual basis of papers submitted to court, Fed.R.Civ.P. 11; (2) erred in determining that Business Guides failed to conduct such a reasonable inquiry; and (3) abused its discretion in dismissing Business Guides's action as part of the sanction imposed. In addition, Chromatic urges us to invoke Rule 11 to require Business Guides to reimburse Chromatic for its costs of defending this appeal. The district court had jurisdiction pursuant to 28 U.S.C. § 1338(a). We have jurisdiction over this timely appeal

pursuant to 28 U.S.C. § 1291. We affirm in part, reverse in part, vacate in part, and remand.

I

Business Guides is a subsidiary of Lebhar-Friedman, Inc., a leading publisher of trade journals and magazines in the United States. Business Guides publishes 18 different directories for specialized areas of retail trade. Since 1983, Business Guides has published a directory for computer products and services. This action was based on allegations that Chromatic copied the 1984 edition of Business Guides's computer products and services directory (Directory)

[1] To protect itself against copyright infringement by competitors, Business Guides intentionally plants incorrect information, known in the industry as "seeds," throughout its directories. Business Guides uses two types of seeds. "Type A" seeds are wholly fictitious entries, i.e. businesses which do not exist. "Type B" seeds are partially altered listings, containing minor errors such as transposed numbers in an address or misspelled names. The appearance of one or more seeds in a competitor's publication is strong evidence that copyrighted material has been appropriated.

Business Guides maintains a "master seed list" for each directory it publishes. Normally this master list, which identifies Type A and B seeds separately, is prepared before publication and its seeds are inserted just before the final printing. In preparing its 1984 master list, however, Business Guides did not follow its usual practice. First, the 1984 master list was prepared almost seven months *after* the publication of the Directory. More importantly for our purposes, Business Guides employed a flawed method of compiling the 1984 master list. This flawed method spurred this lawsuit and, ultimately, produced the Rule 11 sanctions now before us.

Because of a concern that the Directory contained insufficient Type A seeds to substantiate copying, Business Guides directed Burdick, one of its employees, to locate examples of a new form of Type B seed. The new kind of Type B seed would consist of

unintentional typographical errors which had shown up in the final version of the Directory. To locate such errors, Burdick compared the final Directory against initial questionnaires used by Business Guides to gather information from the listed companies. The questionnaires are prepared by Lambe, the Director of Research for Business Guides. When Burdick found a disparity between the information listed in the questionnaires and the final Directory, she recorded this on the master list as a Type B seed. This method, however, erroneously assumed that the information on the questionnaires was correct. In fact, information on the questionnaires was frequently revised by Business Guides employees in the proofreading stage. Thus, the 1984 master list of purported errors contained numerous Type B seeds which were factually accurate. The presence of similar listings in competitors' directories would therefore indicate accurate research rather than any copyright infringement of Business Guide's directory.

On October 31, 1986, Business Guides filed a complaint against Chromatic and Shipp, alleging copyright infringement, conversion, and unfair competition. Chromatic publishes a competing directory of computer software dealers. Business Guides sought, among other prayers, a temporary restraining order (TRO) to prevent Chromatic from displaying its directory at an upcoming important trade show. Business Guides's counsel was the law firm of Finley, Kumble, Wagner, Heine, Unterberg, Manley, Myerson & Casey (Finley Kumble).

Business Guide's complaint identified ten seeds in Chromatic's directory which allegedly had been copied. In support of its application for a TRO, Business Guides submitted various affidavits prepared by Finley Kumble. Among these was the affidavit of Burdick, which identified the ten seeds but did not specify what was incorrect about them. The district court allowed the affidavits to be filed under seal, accepting Business Guides's contention that if the information contained in the affidavits were revealed to the public, Business Guides's ability to catch copyright violators would be impaired.

A hearing on the TRO was scheduled for November 7, 1986. Three days before the hearing, the district judge's law clerk telephoned Finley Kumble and requested more specific informa-

tion regarding the ten seeds. The law clerk asked Finley Kumble to specify what was incorrect about each entry. Finely Kumble then contacted Lambe and requested this additional information. This was apparently the first time Finley Kumble asked for details about the ten "seeds."

Lambe reviewed the 1984 master list and provided Finley Kumble with the requested details. Lambe did not attempt to verify the information by calling the companies listed. Nor did he attempt to obtain the original questionnaires, since they were located in a warehouse in New York and the hearing was only three days away. Lambe did, however, check the accuracy of the seeds' information against subsequent editions of Business Guides's directory. He also checked the zip codes of the listings by consulting a zip code directory. As a result of his investigation, Lambe determined that either three or four of the ten seeds (the record is not clear) in fact contained *correct* information. After Lambe relayed this information to Finley Kumble, the later informed the court that Business Guides was retracting its claim of copying as to three of the ten seeds. In addition to retracting the three seeds, Finley Kumble provided the court with the requested specific information regarding the remaining seven seeds.

Concerned about the accuracy of the remaining seeds in light of (1) the retractions and (2) Chromatic's perceived apparent inability to respond to the allegations in the sealed affidavits, the district court law clerk took steps to verify the remaining seeds. By spending approximately one hour telephoning the companies reflected in the remaining seeds, the clerk determined that all but one of the seeds actually contained correct information.

Finley Kumble submitted supplemental materials to the court on November 7, including a supplemental affidavit of Lambe, prepared by the firm, reflecting the additional information uncovered in Lambe's investigation. Finley Kumble presented Lambe's declaration to him on the morning of the November 7 hearing. Lambe had several hours to review his affidavit. He made one correction, crossing out mention of a fourth seed which he had determined did reflect accurate information but which Finley Kumble had not retracted. Lambe then executed the affidavit.

On November 7, the court, in light of the inaccuracies in Business Guides's papers, denied Business Guides's application for a TRO, stayed further proceedings (including discovery), and referred the matter to a magistrate for a determination of whether Rule 11 sanctions should be imposed on Finley Kumble or Business Guides.

The district court summarized the subsequent sanction proceedings before the magistrate as follows:

> The Chief Magistrate conducted two evidentiary hearings, one in December 1986 and one in January 1987. The first hearing was ordered to determine whether plaintiff's counsel Finley Kumble should be sanctioned pursuant to Fed.R. Civ.P. 11. The second hearing was ordered to determine whether Business Guides itself should be subject to sanctions pursuant to Fed.R.Civ.P. 11. At both hearings the parties were represented by Mr. Ephraim Margolin ("Margolin"), a local San Francisco defense attorney.
>
> On April 3, 1987, Chief Magistrate Woelfen recommended that sanctions be imposed against both Business Guides and Finley Kumble. The Chief Magistrate recommended that Business Guides, but not Finley Kumble, be held responsible for filing the inaccurate TRO papers. The Chief Magistrate further recommended that both Business Guides and Finely Kumble be sanctioned for their conduct in defending the sanctions proceedings. The Chief Magistrate doubted the good faith of the parties' representations that the factual errors in the affidavit were attributable to coincidences. . . .
>
> The parties, represented by new and separate counsel, filed objections to the April 3 report. Business Guides based its objection on its allegation that new evidence, not previously presented to the Chief Magistrate, was fundamental to a correct understanding of the circumstances of this case. This court did not rule on the objections, but referred the matter back to the Chief Magistrate for a hearing on the new evidence and potential reconsideration of his recommendations.

> The Chief Magistrate conducted a third evidentiary hearing on July 9, 1987. Representatives from Business Guides and Finley Kumble were present as well as their respective new counsel.

Business Guides v. Chromatic Communications, Inc., 119 F.R.D. 685, 687 (D.C. Cal.1988) *(Business Guides I)*. The new information presented to the magistrate at the July 9 hearing was simply a full explanation, for the first time, of why the "seeds" had in fact contained accurate information. At the two earlier hearings, Business Guides had not discovered, and so could not explain, the faulty method used to compile the 1984 master seed list. Instead, Business Guides had implausibly argued that the accuracy of the allegedly inaccurate information was coincidental.

Id. at 689.

Based on the third evidentiary hearing, the magistrate, on September 14, 1987, issued a revised report and recommendation regarding sanctions.

> In this report, the Chief Magistrate agreed with Business Guides that the evidence not previously before him was fundamental to a correct understanding of the case. The Chief Magistrate found that the new explanation for the occurrence of inaccuracies, the one the parties presented at the third evidentiary hearing, was reasonable. The Chief Magistrate stated that he no longer believed that either Business Guides or its counsel took part in any intentional misrepresentation or cover-up. The Chief Magistrate did, however, recommend that sanctions be imposed against both parties for their conduct.
>
> The Chief Magistrate found sanctions appropriate against Business Guides because "they failed to conduct a proper inquiry, resulting in the presentation of unreasonable and false information to the court." The Chief Magistrate found that Business Guides used materials they knew or should have known were unreliable for the purpose of creating evidence of copyright infringement.

> The Chief Magistrate found that sanctions were not appropriate against Finley Kumble in connection with the initial filing of the TRO application. The Chief Magistrate instead faulted Finley Kumble (along with Business Guides) for its action a few days after the initial papers were filed. The Chief Magistrate found that both Business Guides and Finley Kumble were put on notice that the court was conducting further inquiry into the factual allegations contained in their TRO papers. In response to an inquiry of the court, one of Finley Kumble's attorneys discovered and removed some of the false material in the affidavit. The Chief Magistrate found that at this point both parties had an obligation to conduct further inquiry into the accuracy of all the remaining material in the affidavit. This the parties failed to do.
>
> The Chief Magistrate also recommended that sanctions be imposed against both parties for their conduct in the defense of the sanctions proceedings. The Magistrate determined that no reasonable person would have been satisfied with the [initial] explanations the parties offered with regard to the inaccuracies present in their papers.

Id. at 687-88 (citation omitted).

Business Guides and Finley Kumble filed objections to the magistrate's revised report, arguing that Rule 11 sanctions were inappropriate under the circumstances. The district judge rejected these objections and adopted the magistrate's findings of fact and recommendations. *id.* at 688, 691.

The district judge agreed with the magistriate that (1) Business Guides violated Rule 11 in filing the TRO application; (2) Business Guides and Finley Kumble violated Rule 11 by failing, after the initial filing of the TRO, to conduct a reasonable inquiry into the facts even though they were put on notice of inaccuracies; and (3) Business Guides and Finley Kumble violated Rule 11 at the first two sanction hearings before the magistrate, *Id.* at 689. The district court rejected Business Guides's argument that oral representations, such as those made to the magistrate at the first two hearings, cannot be the basis for

Rule 11 sanctions. *Id.* at 690. Thus, the district court adopted three separate bases for finding a violation of Rule 11. Finally, the district judge unsealed the record and stayed imposition of the sanctions for thirty days, apparently in order to allow Chromatic to request particular sanctions. *Id.* at 691.

Chromatic then filed a motion for sanctions, which Business Guides opposed. In a decision issued August 5, 1988, the district court ruled on the motion. *Business Guides, Inc. v. Chromatic Communications Enterprises,* 121 F.R.D. 402 (N.D. Cal.1988) (*Business Guides II*). By the time this decision was issued, Finley Kumble had filed for bankruptcy, and Chromatic had withdrawn the part of its Rule 11 motion which applied to the law firm. The district court accepted this withdrawal and issued its ruling without prejudice to Chromatic's right to "pursue a sanctions award against Finley Kumble should its legal status change." *Id.* at 403; *see also id.* at 405. Thus, whether Finley Kumble violated Rule 11 did not figure in the district court's ultimate decision and is not an issue on appeal.

The district court also made further factual findings regarding the one remaining allegedly accurate seed, concluding on the basis of Chromatic's evidence that Chromatic did not copy this seed. *See id.* at 403-04. In addition, the district court rejected Business Guides' argument that it was in fact being sanctioned for the preparation of its master seed list in 1984, and that Rule 11 did not cover such conduct. *Id.* at 404.

Having reaffirmed its decision to impose Rule 11 sanctions, the district court next considered what sanctions to impose upon Business Guides. The court first imposed a sanction of $13,865.66 for Chromatic's legal expenses incurred in defending against the frivolous action and in bringing the motion for sanctions. *Id.* at 405. The court then considered, but refused to award, monetary sanctions based upon Chromatic's alleged "business losses" suffered as a consequence of the lawsuit. *Id.* at 405-06. Next, though acknowledging that it was a "severe sanction," the district court ordered dismissal with prejudice of Business Guide's action. *Id.* at 406. The court reasoned that dismissal was warranted in light of its conclusion that the remaining seed was not copied by Chromatic, and because of "the rather remarkable circumstances of

this case, and the serious consequences of Business Guides' improper conduct." *Id.* Finally, the court considered but rejected the possibility of ordering Business Guides to reimburse the public fisc for the cost of the court's time. *Id.* The court reasoned that the deterrent purpose of Rule 11 was adequately served by the monetary sanction and dismissal of the action. From this order of sanctions and dismissal, Business Guides appeals.

II

We review de novo the district court's determination, based on undisputed facts, that conduct constitutes a violation of Rule 11. *Zaldivar v. City of Los Angeles,* 780 F.2d 823, 828 (9th Cir.1986) (*Zaldivar*). The appropriateness of the sanction imposed is reviewed for abuse of discretion. *Golden Eagle Distributing Corp. v. Burroughs Corp.,* 801 F.2d 1531, 1538 (9th Cir.1986) (*Golden Eagle*).

Business Guides challenges the district court's imposition of Rule 11 sanctions on two grounds: the district court erred in (1) applying to Business Guides, a represented party, an *objective* standard of "reasonable inquiry" into the factual basis of papers submitted to court; and in (2) determining that Business Guides failed to conduct a reasonable inquiry. Business Guides also contends that the district court abused its discretion in dismissing Business Guides's action as part of the Rule 11 sanction imposed. Chromatic requests us to impose additional Rule 11 sanctions upon Business Guides to compensate Chromatic for its costs of defending this appeal and to preserve the deterrent effect of the sanction. We address these arguments in turn.

A.

We first consider Business Guides's argrument that the district court erroneously applied an objective standard of reasonable factual inquiry to a represented party. This is a purely legal question involving construction of Rule 11. We therefore review it de novo. *United States v. McConney,* 728 F.2d 1195, 1201 (9th Cir.) (en banc), *cert. denied,* 469 U.S. 824, 105 S.Ct. 101, 83 L.Ed.2d 46 (1984).

Rule 11 was amended significantly in 1983. The purpose behind the 1988 Amendments was to "revitalize the Rule by encouraging the use of sanctions where appropriate." *Zaldivar*, 780 F.2d at 829; *see also* Fed.R.Civ.P. 11 advisory committee note, *reprinted in* 97 F.R.D. 165, 198 (1983) (Committee Note) ("The new language is intended to reduce the reluctance of courts to impose sanctions"). Before its amendment, Rule 11 had been used infrequently. *See* Risinger, *Honesty in Pleading and its Enforcement. Some "Striking" Problems with Federal Rule of Civil Procedure 11*, 61 Minn.L.Rev. 1, 34-37 (1976) (only 23 reported cases in which parties sought sanctions between 1938 and 1976). Since 1983, under Rule 11's broader provisions for imposing sanctions for frivolous litigation, Rule 11 litigation has become a veritable cottage industry. *See Golden Eagle*, 801 F.2d at 1537.

At the heart of revitalized Rule 11 are its enlarged standards of sanctionable conduct for both attorneys and their clients. Under the amended rule there are basically three types of submitted papers which warrant sanctions: factually frivolous (not "well grounded in fact"); legally frivolous (not "warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law"); and papers "interposed for an improper purpose." Fed.R.Civ.P. 11. The amended rule also requires that a "reasonable" prefiling inquiry be conducted into the law and facts. It also *requires* judges to impose sanctions for any violation of the rule's standards while allowing judges considerable discretion in the choice of what sanction is appropriate.

In this circuit and others, courts have repeatedly emphasized that amended Rule 11 imposes an *objective* standard of conduct. *See. e.g. In re Disciplinary Action against Mooney*, 841 F.2d 1003, 1005 (9th Cir.1988) (*Mooney*) ("The requirements of Rule 11 are measured by an objective standard. Subjective good faith is not relevant."); *Unioil v. E.F. Hutton & Co., Inc.*, 809 F.2d 548, 557 (9th Cir.1986) (*Unioil*), *cert. denied*, 484 U.S. 822, 108 S.Ct. 83, 98 L.Ed.2d 45 (1987); *Golden Eagle*, 801 F.2d at 1538; *Zaldivar*, 780 F.2d at 829 ("The new text represents an intentional abandonment of the subjective focus of the Rule in favor of an objective one.") *Eastway Construction Corp. v. City of New York*, 762 F.2d 243, 253 (2nd Cir.1985) ("Simply put, subjective good faith no longer provides the safe harbor it once did."), *cert. denied*, 484 U.S. 918, 108 S.Ct. 269, 98 L.Ed.2d 226 (1987); *see also* Schwarzer, *Sanctions Under the New Federal Rule 11 — A Closer Look*, 104 F.R.D. 181, 187 (1985) ("There is no room for a pure heart, empty head defense under Rule 11."). However, these cases involved sanctions imposed on attorneys rather than represented parties.

[2] The issue we face is whether Rule 11 prescribes a different standard of "reasonable inquiry" into the facts for represented parties than for attorneys. This is an issue of first impression in this circuit.

We begin with the language of Rule 11. Amended Rule 11 provides in part:

> Every pleading, motion, and other paper of a party represented by an attorney shall be signed by at least one attorney of record in the attorney's individual name, whose address shall be stated. A party who is not represented by an attorney shall sign the party's pleading, motion or other paper and state the party's address. . . . The signature of an *attorney or party* constitutes a certificate by the signer that the signer has read the pleading, motion, or other paper; *that to the best of the signer's knowledge, information, and belief formed after reasonable inquiry it is well grounded in fact* and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law, and that it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation. If a pleading, motion or other paper is not signed, it shall be stricken unless it is signed promptly after the omission is called to the attention of the leader or movant. If a pleading, motion or other paper is signed in violation of this rule, *the court*, upon motion, or upon its own initiative, *shall impose upon the person who signed it, a represented party, or both*, an appropriate sanction, which may include an order to pay to the other party or parties the amount of the reasonable expenses incurred because of the

filing of the pleading, motion, or other paper, including a reasonable attorney's fee.

Fed.R.Civ.P. 11 (emphasis added). As the highlighted language demonstrates, Rule 11's language provides no support for Business Guides's claim that represented parties are not subject to an objective standard of reasonableness. To begin with, the rule clearly authorizes, indeed requires, a judge to sanction a represented party for violations. Significantly, the rule draws no distinction between the state of mind of attorneys and parties. There is nothing in the rule to suggest that a represented party may only be sanctioned for bad faith. On the contrary, the rule, by requiring any "signer" of a paper (attorney *or* party) to conduct a "reasonable inquiry," would appear to prescribe similar standards for attorneys and represented parties.

Nor does the Advisory Committee Note to Rule 11 provide solid support for Business Guides's suggested interpretation. As for the amended rule's new, explicit authorization to sanction clients, the Committee Note states that "[e]ven though it is the attorney whose signature violates the rule, it may be appropriate under the circumstances of the case to impose a sanction on the client." *See* Committee Note, 97 F.R.D. at 200, *citing Browning Debenture Holders' Committee v. DASA Corp.*, 560 F.2d 1078 (2d Cir.1977) *(Browning)*. The Committee Note does not convey an intention to apply different reasonable inquiry standards to attorneys and represented parties. On the contrary, the Committee Note reflects an intention to go beyond a bad faith standard for violations:

> The amended rule attempts to deal with the problem [of courts' reluctance to impose sanctions] by *building upon and expanding* the equitable doctrine permitting the court to award expenses, including attorney's fees, to a litigant whose opponent acts in *bad faith* in instituting or conducting litigation.
>
> . . . .
>
> The new language stresses the need for some prefiling inquiry into both the facts and the law to satisfy the affirmative duty imposed by the rule. The standard is one of reasonableness under the circumstances. This standard is *more stringent than the original good-faith formula* and thus it is expected that a greater range of circumstances will trigger its violation.

97 F.R.D. at 198-99 (emphasis added) (citations omitted). It appears that the drafters intended to expand the scope of Rule 11's coverage beyond mere bad faith to encompass certain *objectively* unreasonable submissions and prefiling inquiries.

Business Guides suggests that we adopt the rule announced by the Second Circuit in *Calloway v. Marvel Entertainment Group*, 854 F.2d 1452 (2d Cir.1988) *(Calloway)*, *cert. granted on other grounds*, ____ U.S. ____, 109 S.Ct. 1116, 103 L.Ed.2d 179 (1989). The court held in *Calloway* that "an 'objectively reasonable test' . . . is appropriate only in evaluating the conduct of attorneys under Rule 11, not the conduct of parties represented by attorneys." *Id.* at 1474. The court explained that "a party represented by an attorney should not be sanctioned for papers signed by the attorney unless the party had actual knowledge that filing the paper constituted wrongful conduct." *Id.* The *Calloway* rule has been applied within the Second Circuit. *See, e.g., Greenberg v. Hilton International Co.*, 870 F.2d 926, 934 (2d Cir.1989); *Quadrozzi v. City of New York*, 127 F.R.D. 63, 79 (S.D.N.Y. 1989); *Alberts v. Wall Street Clearing Corp.*, 1989 WL 88585, 1989 U.S. Dist. LEXIS 7945, at 6 n. 1 (S.D.N.Y. July 13, 1989). In contrast to *Calloway*, the Fourth Circuit appears to apply an objective standard to represented parties' prefiling inquiry into facts. *See Cleveland Demolition Co. v. Azcon Scrap Corp.*, 827 F.2d 984, 987-88 (4th Cir.1987); *see also Portnoy v. Wherehouse Entertainment Co.*, 120 F.R.D. 78, 74 (N.D.Ill. 1988).

In rejecting an objective reasonableness standard of inquiry for represented parties, the Second Circuit in *Calloway* offered two reasons. First, the court reasoned that "[a]s licensed professionals and officers of the court, attorneys are expected to measure up to minimal standards of professional competence under the Rule and thus may not excuse their conduct on the ground that they were acting in good faith." 854 F.2d at 1474. Second, the court deemed significant the Committee Note's citation to a prior Second Circuit case, arguing that "[a]s guidance, the Committee cited *Browning Debenture Holders' Committee v. DASA Corp.*,

560 F.2d 1078 (2d Cir.1977), a case holding that a represented party should not be held liable for wrongful conduct by attorneys unless the party was personally aware of or responsible for the conduct." *Id.*

We do not agree with the Second Circuit's reasons for adopting a subjective standard for represented parties. *Calloway's* first rationale — that attorneys, as licensed professionals, should be held to a higher standard of conduct — is a factor which the rule already takes into account. As the Committee Note instructs, "[t]he standard [of reasonable inquiry] is one of reasonableness *under the circumstances.*" Committee Note, 97 F.R.D. at 198 (emphasis added). Obviously, what is objectively reasonable for a client may differ from what is objectively reasonable for an attorney. Moreover, the Committee Note instructs that willfulness or bad faith should be considered by the sanctioning judge in setting the appropriate sanction once it has been determined that a violation has occurred. *See id.* at 200 ("The reference in the former text to willfulness as a prerequisite to disciplinary action has been deleted. However, in considering the nature and severity of the sanctions to be imposed, the court should take account of the attorney's or party's actual or presumed knowledge when the pleading or paper was signed."). Finally, the Second Circuit's "licensed professional" argument has greater force in cases involving failures to conduct reasonable prefiling inquiries into the *law.* Where a violation occurs because of failure to make a reasonable inquiry into the *factual* underpinnings of a paper or pleading, the client may be in an equal or better position than the lawyer. This is not to say that the lawyer has only a minimal or secondary obligation to investigate the facts provided by the client — only that the client shares this obligation. Here, Business Guides was obviously in a superior position to understand its "seeding" system than was Finley Kumble.

We also do not read the Committee Note's reference to *Browning* as reflecting an intent to require a showing of bad faith when imposing Rule 11 sanctions on parties. The Committee Note states:

> Even though it is the attorney whose signature violates the rule, it may be appropriate under the circumstances of the case to impose a sanction on the client. See *Browning Debenture Holders' Committee v. DASA Corp., supra.* This modification brings Rule 11 in line with practice under Rule 37, which allows sanctions for abuses during discovery to be imposed upon the party, the attorney, or both.

Id. at 200. This paragraph, like the two paragraphs in the Committee Note immediately preceding it, explains a change in Rule 11's text which merely makes explicit the authorization for a particular sanctioning practice which some courts, prior to the amendment, had interpreted the prior version of the rule to allow. *See also id.* ("Courts currently appear to believe that they may impose sanctions on their own motion. Authority to do so has been made explicit. . . . ") (citation omitted); *id.* ("If the duty imposed by the rule is violated, the court should have the discretion to impose sanctions on either the attorney, the party the signing attorney represents, or both . . . and the new rule so provides. Although Rule 11 has been silent on this point, courts have claimed the power to impose sanctions on an attorney personally. . . . The amended rule should eliminate any doubt as to the propriety [of this practice].") (citations omitted). Thus, the Committee Note cites to *Browning* only as an example of a practice which the rule, as amended, explicitly authorizes — imposing a sanction upon a client.

The Second Circuit's conclusion that the Committee Note, by citing *Browning,* demonstrated an intent for a subjective standard to apply to represented parties is flawed for several other reasons as well. First, the fact that *Browning* required subjective bad faith is unexceptional; *every* case cited by the Committee Note required subjective bad faith as a prerequisite to Rule 11 sanctions. The objective standard did not exist prior to the 1983 amendments. Second, *Browning* itself did not involve any failure by the client or attorney to investigate the facts giving rise to the action. Instead, *Browning* involved a sanction for improper purpose. The district court in *Browning* had held that the plaintiffs "had acted in bad faith in instituting and maintaining this action" because plaintiffs' purpose was to obtain a reduction in the conversion price of certain debentures rather than to vindicate their legal rights. *Browning,* 560 F.2d at 1088.

Based on our reading of the text of Rule 11 and the Committee Note, we agree with the Fourth Circuit and conclude that represented parties should be held to an objective standard of "reasonable inquiry" into the facts. *See* Note, *A Uniform Approach To Rule 11 Sanctions*, 97 Yale L.J. 901, 915 (1988) ("If a client knowingly provides false facts, or provides facts that the client *should have known were false*, then the client should be sanctioned.") (footnotes omitted) (emphasis added). Our holding is consistent with our repeated statements, albeit in slightly different contexts, that Rule 11 as amended imposes an objective standard of conduct. *See Mooney*, 841 F.2d at 1005; *Unioil*, 809 F.2d at 557; *Golden Eagle*, 801 F.2d at 1538; *Zaldivar*, 780 F.2d at 829. Even the "improper purpose" prong of Rule 11, which requires sanctions for submissions "interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation," Fed.R. Civ.P. 11, has been interpreted in this circuit to impose an objective standard. *See Zaldivar*, 780 F.2d at 832 ("Harassment under Rule 11 focuses upon the improper purpose of the signer, *objectively tested*, rather than the consequences of the signer's act, subjectively viewed by the signer's opponent.") (emphasis added).

In addition, it is settled that pro se litigants are held to an objective standard of reasonableness under Rule 11. *See* Committee Note, 97 F.R.D. at 199. The Committee Note suggests that "[a]lthough the standard is the same for unrepresented parties, . . . the court has sufficient discretion to take account of the special circumstances that often arise in *pro se* situations." *Id.* Mention of the court's "discretion" merely acknowledges that (1) what is objectively reasonable for a pro se litigant and for an attorney may not be the same, and (2) the pro se status of a violator may be relevant to the court's discretionary choice of the appropriate sanction in a given case. We fail to see why represented parties should be given the benefit of a subjective bad faith standard whereas pro se litigants, who do not enjoy the aid of counsel, are held to a higher objective standard.

Our holding is also consistent with the primary purpose behind Rule 11: deterence of frivolous litigation. *See In re Yagman*, 796 F.2d 1165, 1184 (9th Cir.) (deterrence "paramount" and "overriding" purpose of Rule 11), *amended*, 803 F.2d 1085 (9th Cir.1986), *cert. denied*, 484 U.S. 963, 108 S.Ct. 450, 98 L.Ed.2d 390 (1987). An objective standard for represented parties will ensure greater vigilance to investigating factually baseless claims. *See also Zaldivar*, 780 F.2d at 829 ("Our conclusion that subjective bad faith is not an element to be proved under present Rule 11 is consistent with the advisory committee's purpose to revitalize the Rule by encouraging the use of sanctions where appropriate.") (attorney sanctions). Subjective bad faith is more difficult to demonstrate, and efforts to uncover it can spawn satellite litigation.

[3] In holding that an objective standard applies to lawyers and represented parties alike, we do not suggest that what is a "reasonable" inquiry for an attorney is also a "reasonable" inquiry for a client. As mentioned above, Rule 11's objective reasonableness standard "is one of reasonableness under the circumstances." Committee Note, 97 F.R.D. at 198; *see also id.* at 199 ("[W]hat constitutes a reasonable inquiry may depend on such factors as how much time for investigation was available to the signer . . . ").

B.

Having determined that the district court correctly chose to apply an objective standard of reasonable inquiry to Business Guides, we now consider whether Business Guides violated that standard.

The district court agreed with the magistrate that Business Guides had violated Rule 11 by failing to conduct a reasonable factual inquiry on three separate occasions: (1) before filing the initial TRO papers, (2) before submitting Lambe's supplemental affidavit on November 7, and (3) before appearing at the first two hearings in front of the magistrate. *Business Guides I*, 119 F.R.D. at 689.

[4] We agree with the district court that the first two instances of conduct violated Rule 11. Business Guides is a sophisticated business entity that has extensive experience with copyright litigation. Its papers repeatedly characterize it as a pioneer in the

seeding method, which Business Guides's parent company, Lebhar-Friedman, has employed for over 40 years. It was unreasonable for Business Guides to take no steps whatsoever to verify the ten seeds before filing its papers and request for a TRO. As the district court correctly observed, "Business Guides could easily have checked on the accuracy of the identified seeds (as the court did) prior to submitting the information in an affidavit." *Id.* The district court's law clerk spent one hour and discovered that six of the allegedly false "seeds" in fact contained accurate information. We agree with the district court that Business Guides cannot rely on the alleged accuracy of its seed list as a shield from Rule 11 liability.

[5] We also agree with the district judge that Business Guides and Lambe violated Rule 11 by submitting Lambe's supplemental affidavit on November 7. The district judge's law clerk requested Business Guides's counsel for more specific information on the ten seeds. In searching for this information, Lambe, the Director of Research for Business Guides, also independently attempted to verify the information in the seeds by comparing it against subsequent editions of the Directory and postal zip code lists. Lambe discovered that three or four of the seeds were baseless. The discovery should have spurred Lambe to conduct a much more thorough investigation of the remaining seeds. We reject Business Guides's contention that Lambe should be commended for undertaking his investigation into the seeds' accuracy in the first place. Lambe's inquiry fell short of objective reasonableness under the circumstances of this case.

We also reject Business Guides's attempt to excuse its deficient inquiry by pointing to the short time frame in which it was operating. Business Guides stresses that it was seeking a TRO against Chromatic to prevent Chromatic from displaying its product at an impending trade show. Yet Business Guides apparently suspected Chromatic of copying for two years before this action was filed. Any haste in the initial filing was occasioned by Business Guides's own actions. In addition, we reject Business Guides's argument that Lambe had only two hours to review his affidavit on November 7. Two hours was more time than it took the law clerk to uncover the problems with the seeds. Even so, the

argument is curious that when a party is facing its self-imposed deadline, it is excused from what would otherwise be unreasonable. Nevertheless, Lambe had not just two hours but several days if one considers the time between Lambe's discovery of the inaccurate seeds and the TRO hearing.

[6] Although we agree with two of the district court's bases for imposing Rule 11 sanctions, we agree with Business Guides that the district court erroneously applied Rule 11 to *oral* representations and testimony made to the magistrate. The district court refused to "interpret Rule 11 as permitting oral misrepresentation while forbidding the same misrepresentation in writing." *Business Guides I*, 119 F.R.D. at 690. The court also reasoned that "[t]he arguments advanced in this case were made in connection with pleadings filed with the court and therefore fall within the scope of Rule 11." *Id.* We disagree. The use of Rule 11 is foreclosed by the rule's plain language. Rule 11 applies only to a "pleading, motion, or other *paper*." Fed. R.Civ.P. 11 (emphasis added). In keeping with this focus, Rule 11 imposes a signature requirement. The signature represents a certification by the signer that Rule 11's standards have been met. Sanctions are authorized only "[i]f a pleading, motion, or other paper is signed in violation of this rule," and the court is authorized to sanction only "the person who signed [the paper], a represented party, or both." *Id.*

We are aware of no case which authorizes an application of Rule 11 to oral representations. Nor did the district court cite any authority for this holding. In the absence of contrary binding authority, we follow the plain language of the rule and hold that Rule 11 does not apply to oral arguments or testimony before the court or magistrate. Courts have other weapons besides Rule 11 to combat oral misrepresentations by lawyers or witnesses. Although we reverse the application of Rule 11 to oral representations, we affirm the district court's finding that Rule 11 was violated on the other two grounds.

C.

Business Guides next argues that the district court erred in dismissing its action as part of the Rule 11 sanction imposed. We

review the appropriateness of the particular sanction chosen for abuse of discretion. *Golden Eagle,* 801 F.2d at 1538.

In light of our reversal of one of the three instances of sanctionable conduct found by the district court, we need not address this issue. The district judge's choice of sanction hinged in part upon "the rather remarkable circumstances of this case, and the serious consequences of Business Guides' improper conduct." *Business Guides II,* 121 F.R.D. at 406. We cannot know if the district court will consider a sanction of dismissal appropriate in view of Business Guides' two rather than three violations. We therefore vacate the district court's choice of this sanction and remand for reconsideration in light of this opinion.

D.

[7] Chromatic also seeks Rule 11 sanctions for this appeal. While we may impose Rule 11 sanctions on parties whose papers submitted to this court violate Rule 11, *see Partington v. Gedan,* 880 F.2d 116, 130 & n. 8 (9th Cir.1989); *In re Curl,* 803 F.2d 1004, 1007 (9th Cir.1986), Chromatic does not argue (nor could it successfully) that Business Guides' appellate briefs violate the rule. Instead, Chromatic argues that a party who successfully defends a Rule 11 sanction on appeal should be awarded the costs of attorneys' fees *automatically.* According to this argument, since Chromatic has successfully defended the determination that Rule 11 ultimately was violated, it should be entitled to at least a portion of its fees. Otherwise, its victory of fees in the trial will be dissipated in paying for fees on appeal.

There is ample out-of-circuit authority for this proposition. *See, e.g., Danik, Inc. v. Hartmarx Corp.,* 875 F.2d 890, 897-98 (D.C.Cir.1989) *(Danik); Gorenstein Enterprizes, Inc. v. Quality Care-USA, Inc.,* 874 F.2d 431, 438 (7th Cir.1989) *(Gorenstein); Ballard's Service Center, Inc. v. Transue,* 865 F.2d 447, 450 (1st Cir.1989); *Hays v. Sony Corp. of America,* 847 F.2d 412, 419 (7th Cir.1988); *Muthig v. Brant Point Nantucket, Inc.,* 838 F.2d 600, 607 (1st Cir.1988) *(Muthig); see also Westmoreland v. CBS, Inc.,* 770 F.2d 1168, 1179-80 (D.C.Cir.1985) (*Westmoreland*) (successful appeal from denial of Rule 11 sanctions). In

awarding successful appellees the legal costs of their appeals under Rule 11, these courts have reasoned that such costs are part of the "reasonable expenses *incurred because of*" the frivolous filing in the district court. *Muthig,* 838 F.2d at 607, *quoting* Fed.R.Civ.P. 11 (emphasis added); *see also Danik,* 875 F.2d at 897-98. These courts have concluded that the practice of awarding attorneys' fees on appeal in this situation both preserves the incentives to seek sanctions in the district court and furthers the underlying goals of Rule 11. *Gorenstein,* 874 F.2d at 438; *Muthig,* 838 F.2d at 607; *Westmoreland,* 770 F.2d at 1179.

Were we writing on a clean slate, we might find these arguments persuasive. However, in this circuit the slate is not clean. Business Guides correctly points out that *Orange Production Credit Association v. Frontline Ventures, Ltd.,* 801 F.2d 1581 (9th Cir.1986), requires us to reject Chromatic's request for attorneys' fees on appeal. In *Orange Production,* we rejected the argument that the legal costs of defending an award of Rule 11 sanctions on appeal were costs "incurred because of" the filing in the district court. *Id.* at 1582. We reasoned that "[i]f we were to award sanctions of attorneys' fees on appeal based on this analysis ... then every appellee who succeeded in preserving a favorable trial court award in a Rule 11 case would be entitled to fees on appeal regardless of the substance of the appeal." *Id.* Nor were we swayed by the argument that awarding Rule 11 sanctions to successful appellees would preserve the effectiveness of the sanction awarded in the trial court. *Id.* at 1582-83.

In holding that sanctions were unavailable in this situation, we followed the Fourth Circuit's decision in *Baĉch v. Westinghouse Electric Corp.,* 777 F.2d 165, 175 (4th Cir.1985), *cert. denied,* 476 U.S. 1108, 106 S.Ct. 1957, 90 L.Ed.2d 365 (1986). We also distinguished the District of Columbia Circuit's decision in *Westmoreland* on the grounds that it involved an appeal from the *denial* of Rule 11 sanctions. While our decision in *Orange Production* has been criticized, *see Danik,* 875 F.2d at 898, *Orange Production* remains the law of this circuit. We must therefore reject Chromatic's request for Rule 11 sanctions for this appeal.

We affirm the district court's determination that Business Guides violated Rule 11 by failing to conduct a reasonable prefiling inquiry into the facts before (1) signing the original complaint, and (2) submitting Lambe's supplemental declaration. We reverse, however, its holding that oral representations of Business Guides' employees violated Rule 11. We do not know the impact this will have on the monetary award or dismissal of the action. Therefore, we vacate the order of sanctions and remand to allow the district court to reconsider its choice of sanctions in light of our determination.

AFFIRMED IN PART, REVERSED IN PART, VACATED IN PART, AND REMANDED.

BUSINESS GUIDES, INC.,
Plaintiff,
v.
CHROMATIC COMMUNICATIONS ENTERPRISES, INC. and MICHAEL SHIPP,
Defendants.

No. C 86-6164 SC (FW).

United States District Court,
N.D. California.

Aug. 5, 1988.

Publisher of business directory brought copyright infringement action against competitor. On competitor's motions for sanctions, the District Court, Conti, J., held that publisher of business directory would be required to pay competitor's legal expenses and out-of-pocket costs and its action would be dismissed as Rule 11 sanctions.

Ordered accordingly.

1. Federal Civil Procedure — 2721

Publisher of business directory would be required to pay competitor's legal expenses and out-of-pocket costs, and publisher's copyright infringement action against competitor would be dismissed as Rule 11 sanctions for filing action without reasonable factual inquiry; publisher claimed that false information or "seeds" that appeared in its directory also appeared in competitor's directory, but failed to check accuracy of purported seeds. Fed.Rules Civ.Proc. Rule 11, 28 U.S.C.A.

2. Federal Civil Procedure — 2721

Consequential damages suffered as result of frivolous copyright infringement action could only be sought through collateral action and would not be awarded as Rule 11 sanctions. Fed.Rules Civ.Proc.Rule 11, 28 U.S.C.A.

Heller, Ehrman, White & McAuliffe, San Francisco, Cal., for plaintiff.

Cooper, White & Cooper, San Francisco, Cal., for defendants.

ORDER IMPOSING SANCTIONS

CONTI, District Judge.

On April 12, 1988, this court issued an order adopting the recommendations of Chief Magistrate Woelflen that Business Guides, Inc. ("Business Guides") and its counsel Finley, Kumble, Wagner, Heine, Underberg, Manley, Myerson & Casey ("Finley Kumble") be sanctioned pursuant to Fed.R.Civ.P. 11. The order of the court also unsealed the file and record in the matter, and granted defendants Chromatic Communications Enterprises, Inc. ("Chromatic") and Michael Shipp ("Shipp") thirty days to respond to the court's findings with a motion for sanctions. The matter is currently before the court on defendants' motion for sanctions.

The defendants originally brought this motion for sanctions against both Business Guides and Finley Kumble. Subsequent to the defendants' notice of the motion, this court received a letter from the law firm of Milbank, Tweed, Hadley & McCloy ("Milbank Tweed") informing the court that Finley Kumble had recently dissolved and that the estate was in Chapter 11 bankruptcy proceedings in the United States Bankruptcy Court, Southern District of New York. Milbank Tweed informed the court that it represented the Chapter 11 Trustee for Finley Kumble, and that pursuant to court order, any proceeding to recover a claim against Finley Kumble was stayed under Section 362 of the Bankruptcy Code.

The issue of the applicability of a bankruptcy stay to these proceedings has never been briefed. After consulting with Milbank Tweed, defendants decided to withdraw that part of their motion which applied to Finley Kumble. Defendants' motion is therefore directed only toward Business Guides. The court will accept the representation of Milbank Tweed, as counsel for the trustee in bankruptcy, that any proceedings against Finley Kumble are stayed pursuant to the Bankruptcy Code. The court's disposition of the matter before it does not prejudice defendants' right to pursue a sanctions award against Finley Kumble should its legal status change.

Defendants argue that the action Business Guides brought against them had no basis in fact and was interposed to harrass them. Defendants seek the imposition of sanctions against Business Guides, pursuant to Rule 11, in the form of an award of attorney's fees, damages for loss of business, and an order dismissing the action. Business Guides opposes defendants' motion, arguing that sanctions are inappropriate in the circumstances of this case.

The factual background and law applicable to this matter was set out in detail in the court's April 12, 1988 order. *See Business Guides v. Chromatic Communications Enterprises, Inc.*, 119 F.R.D. 685 (N.D.Cal.1988). In their moving papers, however, defendants have proferred evidence which further develops the factual background of these proceedings. In its order of April 12, 1988, the court explained that of the ten purported "seeds" used in Business Guides' directory, the seeds which allegedly demonstrated copyright infringement, the court could only confirm the falsity of the information given in one seed. 119 F.R.D. at 687. Defendants have now come forward with competent evidence that they did not copy the lone purported seed from Business Guides' directory. Rather, the defendants argue that the remaining seed was "planted" in their directory by Business Guides to investigate their operation.

The seed at issue was originally described by Business Guides as an entity entitled NFR Computer Room, 87-32 253rd St., Bellerose, New York 11426. An individual named Nick Rossini was listed as the President and Buyer of this company. According to plaintiff, Business Guides invented this company, and no such company has ever existed. *See* Declaration of Michael Lambe in Support of Plaintiff's Application for a Temporary Restraining order and for Preliminary Injunction, p. 6, filed with this court on November 7, 1986.

Michael Shipp, the president of Chromatic, has submitted a declaration in which he states "unequivocally" that he never purchased, borrowed, acquired, or ever had in his possession Business Guides' directory prior to the preparation of Chromatic's directory. Declaration of Michael Shipp in Support of Motion for Award of Sanctions, p. 3. Shipp further states

> I have personally reviewed portions of this Court's record, following the unsealing thereof on or about April 12, 1988. From my review of that record, it appears that plaintiff is contending that I copied its publication, and although it originally pointed to ten so-called "seeds" which allegedly prove such copying, that claim is now reduced to a single "seed"; Richard Rossini. From a review of my own records, I have determined that Richard Rossini, doing business as The Answer man, was added to our data base when he ordered one of our directories. Attached hereto as Exhibit "A" is a true and correct copy of his order. Attached hereto as Exhibit "B" is a true and correct copy of his recent order for Micro-Leads. Following our standard practice, I forwarded to Mr. Rossini a questionnaire or survey for completion and return. Attached hereto as Exhibit "C" is a true and correct copy of the completed survey form I received from Mr. Rossini.

Id. pp. 3-4. Exhibit A is a copy of an order for Chromatic's diskette and source book. The form has been filled out with the name of Richard Rossini as president of a company called The Answer Man. The order gives the same New York address that Business Guides states it invented. Exhibit B is a copy of an order for a Chromatic directory with the same name and address filled in as Exhibit A. Exhibit C is a copy of a letter to Nick Rossini from Chromatic's source book asking for any changes to the NFR Computer Listing. The letter appears to reflect a change in the title of Rossini's company to "Rossini's Computer Room." This evidence indicates that some individual or entity other than Chromatic or Shipp was responsible for this seed appearing in Chromatic's directory.

Business Guides makes no attempt to challenge defendants' evidentiary showing. Business Guides neither admits nor denies defendants' contention that the purported seed was planted in Chromatic's directory by Business Guides. In fact, Business Guides' opposition to defendants' motion makes no mention of the Shipp declaration or the exhibits. This court can only interpret Business Guides' silence on this subject as its tacit admission that defendants were not in fact responsible for the appearance of this

purported seed in the Chromatic directory. The court is left to conclude that Business Guides' entire lawsuit has no basis in fact.

Business Guides opposes defendants' motion by arguing that, as a matter of law, it cannot be sanctioned for the use of its master seed list or for the presentation of an incorrect and inadequate explanation during the sanctions proceedings. These are arguments Business Guides has asserted throughout the proceedings. Business Guides also argues that it should not be sanctioned for relying in good faith on its counsel, and that Rule 11 does not authorize consequential damages.

This court has already found that Business Guides violated Rule 11. There is nothing in Business Guides' opposition papers which has persuaded this court that this determination is unsound. The court has already considered and rejected Business Guides' argument that its conduct is not sanctionable as a matter of law. The court, however, takes his opportunity to respond to Business Guides' characterization of the conduct for which it is being sanctioned.

Business Guides argues that

> . . . to hold that the method of preparing the list *in 1984* gave rise to a violation of Rule 11 when the list was relied upon in 1986 is, in effect, to impose upon Business Guides a "continuing duty" to reevaluate or re-check business records. That is inconsistent with a steady line of cases which hold that Rule 11 is only applicable as of the "snapshot" in time when a pleading or other paper is filed. [citations omitted]

Memorandum of Points and Authorities of Business Guides, Inc. in Opposition to Defendants' Motion for Sanctions ("Memorandum of Business Guides"), p. 6. Business Guides is missing the point. The point is that a "snapshot" of the pleadings in this case demonstrates that Rule 11 *was* violated. When the pleadings were filed Business Guides' claims had no basis in fact; there was, and is, no evidence of copyright infringement. Rule 11 does not apply to the manner in which Business Guides prepares its business records. However, the rule does apply to the manner in which Business Guides brings lawsuits. The rule requires that a "reason-

able inquiry" be conducted before embarking on litigation. This Business Guides failed to do. This failure is sanctionable.

Business Guides has also argued that because of the intervening bankruptcy filing by Finley Kumble the burden of any sanction fails entirely on it. Business Guides argues that this is unfair because it was merely relying in good faith on its counsel. Business Guides argues that imposing sanctions on it in these circumstances "is akin to penalizing a patient who, although he has described to his physician his symptoms, failed to diagnose his cancer." Memorandum of Business Guides, p. 12.

The court first states that any decision not to impose sanctions on Finley Kumble is based on the legal effect of the bankruptcy stay and does not reflect a determination by this court that Finley Kumble's conduct was not sanctionable. The court, however, does not accept Business Guides' suggestion that responsibility in this manner is better directed toward its counsel. Both Business Guides and its counsel acted unreasonably throughout this litigation. Furthermore, it was Business Guides' failure to get its facts straight which precipitated this lawsuit. The problem with the commencement of this lawsuit, to use Business Guides' analogy, was not a faulty diagnosis, it was false symptoms.

This case illustrates well the dangers of a party's failure to act reasonably in commencing litigation. Here Business Guides, a sophisticated corporate entity, hired a large, powerful and nationally known law firm to file suit against a competitor for copyright infringement. This competitor happened to be a one-man company operating out of a garage in California. Two years later, after extensive time and effort on the part of the court, the various counsel for Business Guides, as well as various counsel for Business Guides' counsel, it turns out there was no evidence of infringement. The entire lawsuit was a mistake. In the meantime, the objects of this lawsuit have spent thousands of dollars of attorney's fees and have suffered potentially irreparable damage to their business. This entire scenario could have been avoided if, prior to filing the suit, Business Guides simply had spent an hour, like the court's law clerk did, and checked the accuracy of the purported seeds.

This court has already found that Business Guides violated Rule 11; the imposition of sanctions is therefore mandatory. *See Hudson v. Moore Business Forms, Inc.*, 827 F.2d 450, 453 (9th Cir. 1987). The district court has much discretion in tailoring an appropriate sanction for a party guilty of misconduct. "It is well established that courts have the inherent power to impose a variety of sanctions on both litigants and attorneys to regulate their docket, promote judicial efficiency, and deter frivolous filings." *Roadway Express, Inc. v. Piper*, 447 U.S. 752, 764, 100 S.Ct. 2455, 2463, 65 L.Ed.2d 488 (1980). The selection of an appropriate Rule 11 sanction "'is ordinarily left in the first instance to the discretion of the district court and it will not be disturbed on appeal absent a showing of an abuse of discretion.'" *Huettig & Schromm, Inc. v. Landscape Contractors*, 790 F.2d 1421, 1427 (9th Cir. 1986). The language of Rule 11 itself authorizes sanctions in the form of an order to pay the aggrieved party the amount of reasonable expenses incurred because of the filing of the pleading, including a reasonable attorney's fee. Fed.R.Civ.P. 11. Further sanctions can include dismissal of the action with prejudice and entry of judgment by default. *Flaksa v. Little River Marine Construction Co.*, 389 F.2d 885, 887 (5th Cir.), *cert. denied*, 392 U.S. 928, 88 S.Ct. 2287, 20 L.Ed.2d 1387 (1968).

[1] Defendants have submitted declarations which indicate that they have incurred legal expenses and out-of-pocket costs in the sum of $13,865.66 in defending this action and bringing this motion for sanctions. *See* Declarations of Messrs. Michael Shipp and Neil L. Shapiro in Support of Motion for an Award of Sanctions. Business Guides has not challenged the amount of claimed expenses or argued that the expenses were incurred unreasonably. After reviewing the papers filed in connection with this matter, the court finds that these legal expenses and costs were reasonably incurred. The court therefore orders Business Guides to pay defendants $13,865.66 as a sanction, pursuant to Fed. R.Civ. 11.

[2] Defendants have also requested that they be compensated for economic losses suffered as a consequence of Business Guides' commencement of this litigation. Shipp's declaration indicates

that defendants suffered business losses of approximately $39,000 in the form of excess costs and lost profits as a result of the commencement of this lawsuit. The damage to defendants' business reputation and the cost of lost business opportunities is difficult to assess. It may well be that the defendants have suffered irreparable damage.

Defendants, however, have cited no controlling authority in support of their request for an award of consequential damages under Rule 11. The court, while sympathetic to defendants' plight, is not persuaded that such compensation is within the purview of Rule 11. The court is of the opinion that such relief may only be sought through a collateral action. The court therefore declines to order such relief.

Defendants have also sought dismissal of this action as a sanction. The court is mindful that dismissal of an action is a severe sanction. However, it is now evident that this action has no basis in fact. Given the rather remarkable circumstances of this case, and the serious consequences of Business Guides' improper conduct, the court finds that dismissal is warranted. The court therefore orders that this action be dismissed with prejudice.

Finally, the court must decide if any further sanctions should be imposed on Business Guides independently by this court. In its April 12, 1988 order the court expressed its concern that the taxpayers, by bearing the cost of the satellite sanction hearings, have in effect been punished for the parties' misconduct. 119 F.R.D. at 690. The court also stated its intention to impose sanctions on Business Guides and Finley Kumble in an amount which would reasonably reimburse the taxpayers for the cost of the sanction proceedings. *Id.* The court is still concerned with the unfairness of the taxpayers paying for the parties' misconduct. However, in light of the sanctions herein imposed, the court finds that the deterrent purpose of Rule 11 has been satisfied and the imposition of further sanctions is not warranted.

In accordance with the foregoing, the court orders that:

(1) Business Guides is to pay defendants $13,865.66 as a sanction, pursuant to Fed. R.Civ.P. 11; and

(2) The action is dismissed with prejudice.

BUSINESS GUIDES, *Plaintiff,*
v.
CHROMATIC COMMUNICATIONS ENTERPRISES, INC., and
MICHAEL SHIPP,
Defendants.

No. C-86-6164 SC (FW).

United States District Court,
N.D. California.

April 12, 1988.

Publisher sought temporary restraining order for alleged improper copying of one of its business directories. After discovery of inaccuracies in publisher's affidavits supporting temporary restraining order, the District Court, Conti, J., held that: (1) publisher and publisher's attorney acted unreasonably in filing temporary restraining order, where publisher offered inaccurate information in its papers which could easily have been checked on prior to submitting information in affidavit; (2) publisher and its attorney acted unreasonably after initial filing of temporary restraining order, where neither party conducted reasonable investigation into accuracy of information until after it was discovered that there were problems with information; and (3) publisher and its attorney acted unreasonably in defense of sanction proceedings since it was not until after magistrate issued report concerning sanctions that parties uncovered true reason for inaccurate information.

Imposition of sanctions stayed for 30 days.

1. Federal Civil Procedure —2721

Publisher and publisher's attorney acted unreasonably in filing temporary restraining order, and publisher deserved sanctions under Rule 11 for its conduct, where publisher offered inaccurate information in its restraining order papers which could easily have been checked on prior to submitting information. Fed.Rules Civ. Proc.Rule 11, 28 U.S.C.A.

2. Attorney and Client —24
Federal Civil Procedure —2721

Publisher and its attorney acted unreasonably after initial filing of temporary restraining order subjecting both to Rule 11 sanctions; both were put on notice that court was conducting further inquiry into factual allegations contained in temporary restraining order application, and neither conducted reasonable investigation into accuracy of information until after it was discovered that there were problems with information. Fed.Rules Civ.Proc.Rule 11, 28 U.S.C.A.

3. Attorney and Client —24
Federal Civil Procedure —2721

Publisher and its attorney acted unreasonably in defense of Rule 11 sanction proceedings brought for publisher's and attorney's failure to check accuracy of information in affidavit supporting temporary restraining order; it was not until after magistrate issued report concerning sanctions for inaccurate information that publisher and attorney uncovered true reason for inaccurate information. Fed.Rules Civ.Proc.Rule 11, 28 U.S.C.A.

4. Federal Civil Procedure —2721

Rule 11 applies to oral representations and applies to party even if he did not actually sign pleadings as long as attorney who represented him did. Fed.Rules Civ. Proc.Rules 11, 11 note, 28 U.S.C.A.

5. Attorney and Client — 24
Federal Civil Procedure — 2721

Court could impose Rule 11 sanctions, in amount which would reasonably reimburse taxpayers for costs of sanction proceedings, on publisher and its attorney for failing to check accuracy of information supplied in affidavit used to obtain temporary restraining order. Fed.Rules Civ. Proc.Rule 11, 28 U.S.C.A.

Finley, Kumble, Wagner, Heine, Underberg, Manley & Casey, Beverly Hills, Cal., James, Gack & Freeman, Santa Rosa, Cal., McCutchen & Doyle, San Francisco, Cal., for plaintiff.

Cooper, White & Cooper, San Francisco, Cal., for defendants.

ORDER Re: RULE 11 SANCTIONS

CONTI, District Judge.

This action was originally brought by plaintiff Business Guides, Inc. ("Business Guides") against defendants Chromatic Communications Enterprises, Inc. ("Chromatic") and Michael Shipp ("Shipp"). Business Guides alleged copyright infringement and sought an injunction and damages for the alleged improper copying of one of its business directories. The case is currently before the court on the objections of Business Guides and its counsel, Finley, Kumble, Wagner, Heine, Underberg, Manley, Myerson & Casey ("Finley Kumble"), to the recommendations of Chief Magistrate Woelfen that sanctions be imposed against Business Guides and its counsel, pursuant to Fed.R.Civ.P. 11.

I. BACKGROUND

Business Guides is a subsidiary of Lebhar-Friedman, a leading publisher of retail trade magazines and journals. Business Guides publishes directories for different areas of retail trade. In 1983, Business Guides began publishing an annual directory of computer products and services. In an effort to protect its directory from possible copyright infringement, Business Guides planted false information, called "seeds," throughout its directory. The seeds consisted of purposely altered street addresses, zip codes, or purposely mispelled names. These seeds were included in the directories so that, if these false entries were to appear in a competitor's publication, Business Guides would have evidence of copyright infringement.

In November of 1986 Business Guides, through its counsel Finley Kumble, filed this action for copyright infringement and applied for a temporary restraining order ("TRO") from this court. Business Guides believed that defendant had copied its directory and reformatted it as a diskette. Business Guides based this belief on the alleged discovery of its seeds in defendant's diskette. Business Guides submitted affidavits under seal, in support of its application for a TRO, alleging that if the information contained in the affidavits was disclosed to the public, the

effectiveness of the devices used to apprehend copyright violators would be lost. The court ordered the papers filed under seal.

Business Guides' affidavits stated that defendant had copied ten of plaintiff's seeds. One of the affidavits, that of Victoria Burdick ("Burdick") a sales representative for Business Guides, identified the entries containing the seeds in excerpts from both plaintiff's and defendant's directories. Burdick's affidavit did not specifically identify what was incorrect about the seeds.

Prior to the hearing on plaintiff's application for a TRO, the court requested that Finley Kumble provide it with more specific identification of the seeded information. After relaying the court's request to Business Guides, Finley Kumble informed the court that plaintiff retracted its claims of copying as to three of the ten seeds. Finley Kumble then specifically identified the seeded information contained in the remaining seven seeds and provided the alleged "correct" information.

After this retraction, the court proceeded to determine the accuracy of plaintiff's representations. The court was concerned because plaintiff's affidavits were filed under seal, and thus defendants had no opportunity to respond to the allegations. The court called one of the entries which it had been told contained seeded information and discovered the alleged incorrect information was actually correct. The court then called each of the remaining six seeds and discovered that neither plaintiff's nor defendant's directories contained the incorrect information as plaintiff had alleged. Of the three remaining seeds, the court could only determine that one was a true seed, in which the falsity of the information given to the court could be confirmed.

Subsequent to the court's discovery of inaccuracies in plaintiff's affidavits, the court referred the matter to Chief Magistrate Woelfen to conduct an evidentiary hearing concerning possible sanctions.

II. SANCTIONS PROCEEDINGS

The Chief Magistrate conducted two evidentiary hearings, one in December 1986 and one in January 1987. The first hearing was ordered to determine whether plaintiff's counsel Finley Kumble should be sanctioned pursuant to Fed.R.Civ.P. 11. The second hearing was ordered to determine whether Business Guides itself should be subject to sanctions pursuant to Fed.R.Civ.P. 11. At both hearings the parties were represented by Mr. Ephraim Margolin ("Margolin"), a local San Francisco defense attorney.

On April 8, 1987, Chief Magistrate Woelfen recommended that sanctions be imposed against both Business Guides and Finley Kumble. The Chief Magistrate recommended that Business Guides, but not Finley Kumble, be held responsible for filing the inaccurate TRO papers. The Chief Magistrate further recommended that both Business Guides and Finley Kumble be sanctioned for their conduct in defending the sanctions proceedings. The Chief Magistrate doubted the good faith of the parties' representations that the factual errors in the affidavit were attributable to coincidences. The Chief Magistrate also suggested that disciplinary proceedings be instituted against Finley Kumble pursuant to Local Rule 110-7.

The parties, represented by new and separate counsel, filed objections to the April 8 report. Business Guides based its objection on its allegation that new evidence, not previously presented to the Chief Magistrate, was fundamental to a correct understanding of the circumstances of this case. This court did not rule on the objections, but referred the matter back to the Chief Magistrate for a hearing on the new evidence and potential reconsideration of his recommendations.

The Chief Magistrate conducted a third evidentiary hearing on July 9, 1987. Representatives from Business Guides and Finley Kumble were present as well as their respective new counsel. On September 14, 1987, Chief Magistrate Woelfen issued a revised report and recommendation regarding sanctions.

In this report the Chief Magistrate agreed with Business Guides that the evidence not previously before him was fundamental to a correct understanding of the case. The Chief Magistrate found that the new explanation for the occurrence of inaccuracies, the one the parties presented at the third evidentiary hearing, was reasonable. The Chief Magistrate stated that he no

longer believed that either Business Guides or its counsel took part in any intentional misrepresentation or cover-up. The Chief Magistrate did, however, recommend that sanctions be imposed against both parties for their conduct.

The Chief Magistrate found sanctions appropriate against Business Guides because "they failed to conduct a proper inquiry, resulting in the presentation of unreasonable and false information to the court." Magistrate's Revised Report and Recommendations Regarding Rule 11 Sanctions ("Revised Report"), p. 12. The Chief Magistrate found that Business Guides used materials they knew or should have known were unreliable for the purpose of creating evidence of copyright infringement.

The Chief Magistrate found that sanctions were not appropriate against Finley Kumble in connection with the initial filing of the TRO application. The Chief Magistrate instead faulted Finley Kumble (along with Business Guides) for its action a few days after the initial papers were filed. The Chief Magistrate found that both Business Guides and Finley Kumble were put on notice that the court was conducting further inquiry into the factual allegations contained in their TRO papers. In response to an inquiry of the court, one of Finley Kumble's attorneys discovered and removed some of the false material in the affidavit. The Chief Magistrate found that at this point both parties had an obligation to conduct further inquiry into the accuracy of all the remaining material in the affidavit. This the parties failed to do.

The Chief Magistrate also recommended that sanctions be imposed against both parties for their conduct in the defense of the sanctions proceedings. The Magistrate determined that no reasonable person would have been satisfied with the explanations the parties offered with regard to the inaccuracies present in their papers.

Both Business Guides and Finley Kumble have filed objections to the Chief Magistrate's Revised Report. Both parties argue that sanctions are inappropriate in the circumstances of the case. Both parties also argue alternatively that in the event this court finds that the parties have violated Rule 11, the parties have already been punished enough to satisfy the objectives of Rule 11.

III. APPLICABLE LAW

The Federal Rules of Civil Procedure provide, in relevant part:

> The signature of an attorney or party constitutes a certificate by the signer . . . that to the best of the signer's knowledge, information, and belief *formed after reasonable inquiry it is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law*, and it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation. . . . If a pleading, motion, or other paper is signed in violation of this rule, the court, upon motion or upon its own initiative, *shall impose* upon the person who signed it, a represented party, or both, an appropriate sanction, which may include an order to pay to the other party or parties the amount of the reasonable expenses incurred because of the filing of the pleading, motion, or other paper, including a reasonable attorney's fees.

Fed.R.Civ.P. 11 (emphasis added).

The emphasized language was inserted in Rule 11 as part of the extensive amendments to its terms that were adopted in 1983. *See* 2A Moore's Federal Practice § 11.01[3](1985). The primary purposes of these amendments were (1) to substitute an objective standard of reasonableness for the previous subjective "good faith" test, (2) to impose on counsel an affirmative duty of diligent investigation of both the facts and the law bearing on the merits of his pleadings, and (3) to render the imposition of sanctions mandatory rather than discretionary when the standards of the Rule have been violated. Note of the Advisory Committee on the 1983 Amendments, 97 F.R.D. 165, 198 (1983); *Hudson v. Moore Bus. Forms, Inc.*, 827 F.2d 450, 453 (9th Cir.1987); *Golden Eagle Dist. Corp. v. Burroughs Corp.*, 801 F.2d 1531, 1536 (9th Cir.1986); *Orange Prod. Credit Assn. v. Frontline Ventures, Ltd.*, 792 F.2d 797, 800 (9th Cir.1986); *Huettig & Schromm, Inc. v. Landscape Contractors Assn.*, 790 F.2d 1421, 1426 (9th Cir.1986); *Eastway Constr. Corp. v. City of New York*, 762 F.2d 243, 253-54 (2d Cir.1985).

IV. ANALYSIS

In the instant case, Chief Magistrate Woelflan has issued a lengthy, detailed report recommending sanctions against both Business Guides and Finley Kumble. The report is thorough and well reasoned, and the Chief Magistrate is to be commended for his considerable efforts.

Neither party has raised any serious disagreement with the Chief Magistrate's factual findings and the court therefore adopts the statement of facts as presented in the Magistrate's Revised Report.

The standard of conduct under Rule 11 is one of objective reasonableness. Applying this standard to the circumstances of this case, it is clear that both Business Guides and Finley Kumble have violated the Rule.

[1] The court finds that Business Guides acted unreasonably in filing the TRO. It is undisputed that Business Guides offered inaccurate information in its papers. Business Guides could easily have checked on the accuracy of the identified seeds (as the court did) prior to submitting the information in an affidavit. The court finds Business Guides' reliance on the accuracy of their process for preparing "seeds" misplaced. The court rejects any claim that Business Guides conducted a "reasonable inquiry" prior to filing this action. The court therefore adopts the Chief Magistrate's finding that Business Guides is deserving of sanctions for its conduct in connection with the filing of the TRO application.

[2] The court finds that both Business Guides and Finley Kumble acted unreasonably after the initial filing of the TRO. Both parties were put on notice that the court was conducting further inquiry into the factual allegations contained in the TRO application. Neither party conducted a reasonable investigation of the accuracy of the seeded information after it was discovered that there were problems with three of the seeds. The court agrees with the Chief Magistrate that this failure to investigate is sanctionable conduct pursuant to Rule 11. The court therefore adopts the Chief Magistrate's recommendation that Business Guides and Finley Kumble should be jointly sanctioned for this

conduct in connection with the filing of the inaccurate TRO application.

[3] The court also finds that both Business Guides and Finley Kumble acted unreasonably in the subsequent defense of the sanctions proceedings. The parties initially sought to explain the fact that some of the alleged incorrect information was actually correct by arguing the occurrences were coincidental. The parties explained that Business Guides had sent a questionnaire to companies in order to compile its directory, and that some of the information in the questionnaire was incorrect. When Business Guides prepared its seeds, parties explained, it altered the incorrect information in such a way as to make the information correct. The Chief Magistrate summarized this line of defense in his Revised Report:

> At both the December and January hearings, the parties testified plaintiff relied upon the questionnaire, which indicated the spelling was BLEDSOE [one of the "seeds"], for the information presented to the court. They testified that it was only a coincidence that the information represented to the court as incorrect seeded information (BLEDSOE) was actually correct. In my April 8, 1987 Report, I noted that in order for the court to believe defendant's explanation, plaintiff must be able to persuade me that Bledsoe's company incorrectly spelled his name on the questionnaire. More importantly however plaintiff would have had to convince me that it was merely coincidental that plaintiff chose to alter, among thousands of listings contained in the directory, first, this particular listing; second, this particular word in the listing; and third, this particular letter in the word, resulting in an alteration which turned out to be the true spelling of this man's name. I noted plaintiff asked me to believe the occurrence of a very similar coincidence in the COMPUTERLAND seed. I found the occurrence of two such similar and incredible coincidences impossible to believe. Accordingly, I doubted the good faith of the parties' representations and recommended sanctioning them for offering false representations in defense from Rule 11 sanctions. I also suggested that discipline proceedings against Finley,

> Kumble may also be appropriate pursuant to Local Rule 110-7.

Revised Report, pp. 8-9. It was not until after the Chief Magistrate issued his April 3, 1987 report that the parties uncovered the true reason for the inaccurate information.

The Chief Magistrate has concluded that neither Business Guides nor Finley Kumble were engaged in any intentional misrepresentation or cover-up in their sanction defense. The court accepts this determination. The court finds that the arguments presented to the Chief Magistrate at the December and January hearings were wholly unsupportable, and that no reasonable attorney or person could have formed "a reasonable belief, after reasonable inquiry, that the explanations contained in those pleadings and professed at those hearings were well-grounded in fact." *Id.* The court also expresses its agreement with the Chief Magistrate's conviction that "[it] should not take the threatened inposition of sanctions or discipline and contempt proceedings to bring attorneys to fulfill their duties as officers of the court." *Id.* p. 22. The court therefore adopts the Chief Magistrate's recommendation that both parties should be sanctioned for their conduct in defense of the sanction proceedings.

Both Business Guides and Finley, Kumble have argued that the Chief Magistrate's interpretation of Rule 11 is erroneous as a matter of law. Finley Kumble argues

> to the extent the Magistrate's Revised Report holds that Finley Kumble can be sanctioned for making (or failing to make) *oral* representations, the new recommendations are wrong as a matter of law. Rule 11 applies only to certifications of writings .... Indeed, Rule 11 may apply only to the attorney who has actually signed a paper, in which case Finley, Kumble's only possible responsibility may be for the TRO application which the Magistrate found did *not* violate Rule 11.

Finley Kumble's Objections to Magistrate's Revised Report And Recommendations, p. 10, fn. 6. Business Guides similarly argues that "Rule 11 has no application to developments subsequent to

filing the papers at issue." Business Guides' Sealed Objections to Magistrate's Revised Report, p. 8.

[4] The court rejects the parties' interpretation of Rule 11. The parties have not cited to the court controlling authority which indicates the Rule has no applicability to oral representations. The court does not interpret Rule 11 as permitting oral misrepresentation while forbidding the same misrepresentation in writing. The arguments advanced in this case were made in connection with pleadings filed with the court and therefore fall within the scope of Rule 11. The court also rejects the contention that Rule 11 cannot apply to a party if they did not actually sign the pleadings in connection with the sanction proceedings:

> If the duty imposed by [Rule 11] is violated, the court should have the discretion to impose sanctions on either the attorney, the party the signing attorney represents, or both . . ., *and the new rule so provides.*

Fed.R.Civ.P. 11, Note of the Advisory Committee (emphasis added).

[5] Having adopted the Chief Magistrate's recommendation that sactions be imposed against both Business Guides and Finley Kumble, the court must now determine the amount of sanctions. Both parties have argued that in the event the court determines that sanctions are warranted, they have already incurred sufficient expenses in defending this action to serve the Rule 11 purpose of deterring improper conduct. The court is not persuaded by this argument. These sanctions proceedings have occupied an enormous amount of the court's time. Chief Magistrate Woelfen has conducted three evidentiary hearings and has issued two in-depth reports. The Chief Magistrate and his staff have expended well over 180 hours in these satellite proceedings. This court has also dedicated considerable time and effort to these proceedings. This time and effort would have been saved if the parties had acted reasonably in connection with this litigation. It is the taxpayers who are being punished for the parties' misconduct. Therefore the court will impose sanctions in an amount which will reasonably reimburse the taxpayers for the cost of these satellite proceedings.

Before levying sanctions, however, the court will unseal these proceedings and allow the defendants an opportunity to respond to the court's findings, with a motion for sanctions. The court therefore stays the imposition of sanctions and grants defendants thirty (30) days from the date of the filing of this order to file a motion for sanctions.

V. ORDER

In accordance with the foregoing, the court orders that:

(1) the recommendations of the Chief magistrate that sanctions be imposed against Business Guides and Finley Kumble are hereby adopted as the order of this court as set forth in this order;

(2) the objections of Business Guides and Finley Kumble to the recommendations of the Chief Magistrate are denied;

(3) the file in this matter is hereby unsealed; and

(4) the court stays the imposition of sanctions against Business Guides and Finley Kumble; defendants are granted thirty (30) days from the date of the filing of this order to file a motion for sanctions based on the findings of this court.

No. C-86-6164 SC (FW)

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

BUSINESS GUIDES, INC.,
Plaintiff,
v.
CHROMATIC COMMUNICATIONS
ENTERPRISES, INC., and
MICHAEL SHIPP,
Defendants.

MAGISTRATE'S REVISED REPORT AND RECOMMENDATION REGARDING RULE 11 SANCTIONS

I. BACKGROUND

In the underlying action, plaintiff Business Guides is seeking an injunction and damages for copyright infringement involving the alleged improper copying of one of its business directories. Defendant Chromatic Communications has denied infringement and asserts it used only independent sources in preparing its directory.

In the Fall of 1986, plaintiff applied for a temporary restraining order ("TRO") and submitted affidavits under seal alleging that if the information contained in the affidavits was disclosed to the public, the effectiveness of the devices used to apprehend copyright violators would be lost. The trial judge, Honorable Samuel Conti, requested the undersigned magistrate to conduct an evidentiary hearing concerning possible sanctions resulting from plaintiff's misrepresentations to the court in the TRO application. In December 1986 and January 1987, I held two evidentiary hearings. The first was ordered to determine whether plaintiff's counsel, Finley, Kumble, Wagner, Heine, Underberg, Manley, Myerson & Casey ("Finley, Kumble"), should be sanctioned pursuant to Rule 11. The second hearing was ordered to determine whether plaintiff itself should be held subject to Rule 11 sanctions. At both hearings, the parties were represented by Mr. Ephraim Margolin, a local San Francisco defense attorney.

In my Report and Recommendation to Judge Conti, filed on April 3, 1987, I recommended sanctions be imposed against both Business Guides and Finley, Kumble. I recommended that plaintiff, but not Finley, Kumble, be held responsible for filing the faulty TRO. Further, I recommended that both plaintiff and Finley, Kumble be sanctioned for what was at that time perceived to be an intentional cover-up in defense against those sanctions. Both parties, now represented by new and separate counsel, objected to my recommendation and requested Judge Conti disapprove the recommendation for sanctions. Business Guides based its objection on its allegation that new evidence, not previously presented to me, was absolutely fundamental to a correct understanding of the circumstances of this case. Based on Business Guides' representation that such evidence was not previously presented to me, Judge Conti referred the matter back to this court for reconsideration.

On July 5, 1987, this court conducted a third hearing wherein Business Guides' new evidence was adduced. Present at this hearing were representatives from both Business Guides and Finley, Kumble, and their respective new counsel.

I agree with Business Guides that the evidence not previously before me is "absolutely fundamental" to an understanding of what transpired in preparing the TRO application. It is only now, after the many months this controversy has been pending, that I have been presented with a reasonable explanation as to how inaccurate information was originally presented to the court. I no longer believe either Business Guides or its counsel, Finley, Kumble, took part in any intentional misrepresentation or cover-up. I do however find a reasonable inquiry, required by Rule 11, was not conducted by either Business Guides or its counsel, Finley, Kumble.

II.

STATEMENT OF FACTS

Plaintiff publishes directories for different areas of retail trade. In 1983, plaintiff began publishing an annual computer-related directory. Plaintiff testified that due to its concern that a competi-

tor might pirate its directory, it planted false information, called "seeds," throughout its directory. Various street addresses and zip codes were altered by one digit or names were misspelled, so that if the same false information was subsequently printed in a competitor's directory, plaintiff would have strong evidence of copyright infringement.

In early October, 1986 a representative of plaintiff contacted Michael Bamberger, a partner in Finley, Kumble's New York office and told him plaintiff believed that defendant had copied plaintiff's directory and had reformatted it as a diskette. Plaintiff based this belief on the alleged discovery of plaintiff's seeds in defendant's diskette. Bamberger contacted Finley, Kumble's Beverly Hills office and requested assistance from a partner and an associate. Finley, Kumble then prepared a TRO seeking to prevent defendant from marketing its directory at the upcoming Comdex trade show. The associate signed the TRO application. Finley, Kumble prepared affidavits for plaintiff's sales representative, Victoria Burdick, and publisher, Michael Lambe. The affidavits stated defendant had copied plaintiff's seeds. Burdick's affidavit further identified the entries containing the seeds in attached copies of excerpts from both plaintiff's and defendant's directories. Both Burdick and Lambe subsequently testified they reviewed, edited, and executed those affidavits. Both affidavits were filed under seal in support of the TRO application.

In the attached copies to Burdick's affidavit, plaintiff indicated only those entries in the directory that contained the seeds. Plaintiff failed to specifically identify what was incorrect about each entry. Robert Funsten, Judge Conti's law clerk, telephoned the Finley, Kumble associate and asked her to be more specific in her identification of the seeded information. Mr. Funsten wanted to know what was incorrect in each identified entry. The associate requested this information from plaintiff. She then informed Funsten that although plaintiff had asserted in its signed affidavits that defendant copied ten of plaintiff's seeds, plaintiff retracted its claims regarding three of the ten.[1] She then specifically identified the seeded information contained in the remaining seven seeds and provided the alleged "correct" information. For example, she told Mr. Funsten that in one of the entries, COMPUTERLAND,

the street address had been altered. She indicated that the address both plaintiff and defendant had printed in their directories, 3545 Bay Road, was incorrect and had been planted by plaintiff as a seed. She told Funsten the correct address was 3845 Bay Road.

Because the affidavits were made under seal and defendant had no opportunity to respond to plaintiff's allegations, and because of the suspicious retraction of three of the seeds, Funsten called one of the entries which he was told contained seeded information to determine the accuracy of plaintiff's representations. He discovered the alleged incorrect information was actually correct. Funsten proceeded to telephone each of the remaining six seeds. He discovered the information contained in four was entirely correct (i.e., neither plaintiff's nor defendant's directories contained the incorrect information plaintiff said they did). Of the three remaining seeds, one could not be confirmed and falsehood of another was questionable at best.[2] Only one was a verifiable true seed (i.e., the falsity of the information given to the court has been confirmed.[3]

Below are two seeds that plaintiff alleged defendant copied. These two seeds were focused upon at the July 5, 1987 hearing. Included is the information plaintiff presented to the court as accurate and the information the court later determined to be accurate. (For the facts and circumstances of other seeds, see April Report and Recommendation, pages 5-12).

SEED #1: *Computerland*

Plaintiff informed the court that this seed was created by printing Computerland's street address incorrectly: 3545 Bay Road. Plaintiff asserted defendant copied this incorrect information and this is evidence of infringement. The correct address was alleged to be 3845 Bay Road.

Upon further investigation, the court discovered the correct address is indeed 3545 Bay Road, as listed by defendant. At the January hearing, Ms. Burdick testified the information relied upon when making representations to the court came from the actual questionnaire sent to Computerland, i.e., from Computerland itself.

In the April 3, 1987 Report, I noted that in order to believe plaintiff's explanation, I had to first be persuaded that Computerland inaccurately completed the questionnaire; Computerland would have had to mistakenly list its address as 3845 Bay Road, instead of 3545 Bay Road. I noted I had to further be persuaded that plaintiff created 3545 as a seed and it was entirely by coincidence that the seeded address, created by plaintiff, turned out to be the correct address. I found such an incredible set of circumstances impossible to believe.

SEED #2: *Premier Source of Distributing, Inc.*

Plaintiff assserted this seed was created by spelling the company's sales manager's name incorrectly: BLEDSOE. Plaintiff alleged the true spelling was BLODSOE. Plaintiff asserted defendant's inclusion of the incorrect spelling, BLEDSOE, is evidence of infringement. The court discovered the correct spelling of the sales manager's name is BLEDSOE, as defendant listed.

At both the December and January hearings, the parties testified plaintiff relied upon the questionnaire, which indicated the spelling was BLEDSOE, for the information presented to the court. They testified that it was only a coincidence that the information represented to the court as incorrect seeded information (BLEDSOE) was actually correct. In my April 3, 1987 Report, I noted that in order for the court to believe defendant's explanation, plaintiff must be able to persuade me that Bledsoe's company incorrectly spelled his name on the questionnaire. More importantly however plaintiff would have had to convince me that it was merely coincidental that plaintiff chose to alter, among thousands of listings contained in the directory, first, this particular listing; second, this particular word in the listing; and third, this particular letter in the word, resulting in an alteration which turned out to be the true spelling of this man's name. I noted plaintiff asked me to believe the occurrence of a very similar coincidence in the COMPUTERLAND seed. I found the occurrence of two such similar and incredible coincidences impossible to believe. Accordingly, I doubted the good faith of the parties' representations and recommend sanctioning them for offering false representations in defense from Rule 11 sanctions. I also

suggested that discipline proceedings against Finley, Kumble may also be appropriate pursuant to Local Rule 110-7.

The parties then filed objections to the April 3 Report and another hearing was scheduled before me for July 5, 1987. In preparation for this third evidentiary hearing, plaintiff filed a brief and affidavits wherein it explained, for the first time, that the reason inaccurate information had been conveyed to the court stemmed from Victoria Burdick's preparation of the Master Seed List for the 1984 directory. Business Guides explained that normally seeds are intentionally prepared ahead of time, prior to insertion into the publication. The seeds are then listed on the Master Seed List for future reference in assessing whether a competitor had copied seeds. The 1984 seed list, however, was not prepared in this manner. Instead, it was prepared in November 1984, almost seven months after the April publication of the 1984 directory. This was done because plaintiff believed the 1984 edition did not contain enough seeds to substantiate copying in a potential infringement action. In November, 1984, Ms. Burdick was instructed to compare the information on the relevant questionnaires with the information that had been printed in the already-published 1984 directory. Whenever she found a discrepancy between the questionnaire and the directory, she assumed a typographical or editorial error had been made in the directory, rather than the questionnaire, and listed those differences as seeds. Thus, she listed on the 1984 Master Seed List as correct the information that appeared on the questionnaires and listed as seeds the information printed in the 1984 directory.

Business Guides explained that because many of the questionnaires were preprinted by an outside agency (an outside agency printed on questionnaires the company information that had been published in the preceding directory and sent it to that company for the company's verification in order to use that information in the subsequent directory), because information was edited by employees of the listed companies or by plaintiff's telephone staff after preparation of the questionnaires, and because there were many other stages of editing between the time information was printed on the questionnaires and the time the directory was published, reliance on the information from the questionnaires

was an "ill-conceived" idea. They now claim this ill-conceived idea is responsible for the inaccuracies presented to the court in the TRO application.

III. DISCUSSION

After reading the parties' new briefs and listening to their arguments, and after considering the new evidence not presented at the earlier hearings, I withdraw the recommendation presented in my April 3, 1987 Report and Recommendation. I have divided this revised recommendation into two parts. The first consists of my recommendation regarding sanctions for the initial filing of the TRO. The second, my recommendation regarding the parties' conduct in defense from those sanctions.

A. SANCTIONS FOR THE FILING OF THE TRO

Rule 11 of the Federal Rules of Civil Procedure provides in pertinent part:

> The signature of an attorney or party constitutes a certificate by the signer that the signer has read the pleading, motion or other paper; that to the best of the signer's knowledge, information, and belief formed after reasonable inquiry it is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law and that it is not interposed for any improper purpose. . . .

In my April 3, 1987 Report, I recommended Rule 11 sanctions be brought against Business Guides for the inclusion of false statements in the TRO. I still believe this is appropriate. Although I no longer believe Business Guides' actions were "interposed for any improper purpose" because I do not believe they intentionally attempted to deceive the court, I believe Rule 11 sanctions are still appropriate because they failed to conduct a proper inquiry, resulting in the presentation of unreasonable and false information to the court. "Although 'improper purpose' may be an aggravating factor under the new Rule 11, its absence does not insulate from sanctions those who fail the objective standard of reasonableness." *In re Ronco, Inc., et al.*, 105 F.R.D. 493, 498

(N.D. Ill. 1985). I also now recommend, in contrast to my earlier April 3, 1987 Report, that Finley, Kumble be sanctioned for the initial filing of the TRO application. After further consideration, I find reasons to believe both parties acted unreasonably.

First, I believe Business Guides acted unreasonably in its preparation of the 1984 Master Seed List from which the seeds were taken and then used in the TRO application. I therefore find Business Guides acted unreasonably in its *initial* reliance on the accuracy of those seeds. Even Business Guides itself recognizes that post-publication preparation of the seed list was "in hindsight" an ill-conceived idea. I believe the unreliability of the questionnaires and this after publication seed preparation should have been apparent to any reasonable person who knew what Business Guides knew or should have known. Business Guides must have certainly been aware of its own questionnaire preparation and editing process. They knew or certainly should have known the questionnaires they were relying on as accurate went through a rigorous editing process. Their briefs abound in facts explaining the process used in preparing and editing questionnaires and how this process was wrought with errors. Their contention that post-publication seed preparation by relying on the accuracy of the questionnaires was only "in hindsight" an ill-conceived idea therefore does not ring true. I find the preparation of seeds, seven months *after* publication, by relying on the accuracy of questionnaires which Business Guides knew or should have known were unreliable, for the purpose of creating uncontrovertabe evidence of infringement in a potential lawsuit, wholly unreasonable and deserving of sanctions.

I now consider whether Finley, Kumble should also be implicated at this stage of the proceeding. Finley, Kumble had been representing Business Guides for many years. These attorneys testified they relied on plaintiff's information because plaintiff is a sophisticated business entity that had successfully litigated copyright infringement cases in the past. The firm believed there was an urgent need for the TRO in order to prevent defendant from unfairly competing against plaintiff at the upcoming Comdex trade show. Because of the time pressure, an associate worked all weekend preparing the application. We believe that at this stage

in the filing of the TRO, therefore, Finley, Kumble had no reason to suspect Business Guides had prepared their seeds in anything other than a professional and reasonable manner. They therefore had no reason at this time to investigate further by inquiring into the validity and preparation of the seeds. Thus, I do not believe Finley, Kumble should be implicated along with Business Guides in the unreasonable initial reliance on the accuracy of the seeds.

I do believe however Finley, Kumble, along with Business Guides, is deserving of sanctions for the filing of the TRO due to the conduct that occurred, or rather actions that did not occur, days after the papers were filed.

Both Business Guides and Finley, Kumble were put on notice that the court was conducting further inquiry into the factual allegations contained in the TRO application. Three days before the scheduled hearing, Judge Conti's law clerk telephoned one of the Finley, Kumble lawyers requesting further specification of particular information Business Guides claimed defendant had copied.

Mr. Lambe testified that pursuant to this request he conducted a very short investigation of the proffered ten seeds and directed the preparation of the requested information. He stated he had only a "few minutes" to do "last minute checking." (Reporter's transcript, July 5, 1987, ("RT 7/5/87"), p. 39-40.) He testified his investigation consisted of checking only a subsequent edition of the Directory and a zip code book: "just the directories that were in my office and easily at hand." (RT 7/5/87 p. 39.) As a result of this brief investigation, Mr. Lambe discovered that three of ten seeds presented to the court were wrong; they actually contained correct information. Mr. Lambe thus removed these seeds from the application.

I believe that, even assuming the parties were justified in relying on the accuracy of the ten seeds taken from the unusually prepared 1984 seed list at the time of the initial filing of the TRO (which I find Finley, Kumble was but Business Guides was not), upon Mr. Lambe's discovery of three of ten mistaken entries after only a few minutes of investigation, the parties were then obligated to conduct further inquiry into the accuracy of *all* the seeds

presented to the court. I note it took the Judge's law clerk less than an hour to conduct such an investigation. This investigation revealed the errors contained in those seeds and resulted in the Judge's referral to me for an evidentiary hearing regarding the appropriateness of sanctions. Here, the parties had three days to conduct such an investigation and failed to do so. I believe this failure is sanctionable conduct pursuant to Rule 11.

It appears to this court that both Business Guides and Finley, Kumble were on notice and therefore responsible for the failure of an investigation. Finley, Kumble was ware Mr. Lambe's short investigation revealed that three of the ten seeds originally submitted to the court were incorrect. When asked about the crossing out of the three, Lambe told Finley, Kumble two were "soft" and he had some questions about another. (RT 12/86, p. 32, 65). Certainly Finley, Kumble should have at that time been concerned that evidence filed with the court as proof of infringement was only *then*, due to an investigation prompted by an inquiry from the court, being determined questionable. Under these circumstances, Finley, Kumble should have then conducted a further inquiry. I recommend sanctioning both Business Guides and Finley, Kumble jointly and severally for the filing of the TRO. Where there is nothing to indicate the blame should be on either the attorney or the client, sanctions should be imposed against both of them. *Kendrick v. Zandies*, 609 F.Supp. 1162 (D.C. Cal. 1985).

B. SANCTIONS FOR THE SUBSEQUENT DEFENSE AGAINST RULE 11

We next address whether Finley, Kumble or Business Guides should be sanctioned for presenting the arguments they did at the December and January hearings in their subsequent defense against Rule 11 sanctions. Both parties have testified they became aware in early January, prior to the second hearing, that the seeds were prepared seven months after the directory was published. In early January, Victoria Burdick and Michael Lambe met with the Finley, Kumble attorneys in Finley, Kumble's New York offices to prepare for the late January hearing. Michael Lambe testified it was at this meeting he and Ms. Burdick realized the seeds were

prepared after publication. Mr. Gelb sent a letter to Mr. Margolin notifying him of this fact. Although Victoria Burdick was aware of the late preparation in early January, when directly questioned at the late January hearing as to the preparation of the seeds, she did not notify the court of this fact. Mr. Lambe, Mr. Gelb, and Ms. Burdick all testified they did not inform the court of the late preparation because they did not believe it was significant. Mr. Gelb testified he notified Mr. Margolin only because he believed the term "seeds" may be a misnomer in light of the late seed preparation. The parties testified that if they had realized the significance of the seed preparation, they would have had every reason to notify the court.

I find the parties' claims credible that despite their awareness of the *fact* of late preparation, they did not realize the significance of it until the Heller, Ehrman attorneys explained it to them. If they had realized the significance, they surely would have had every reason to present it. I believe, however, that the parties should have realized the significance, and thus informed the court, and their failure to do so was unreasonable. The parties should have conducted the necessary investigation to unearth this new evidence prior to the first two hearings on sanctions. If they had conducted a proper investigation, and notified the court of the new evidence, the third hearing would have been completely unnecessary. Instead of investigating, however, the parties presented wholly unreasonable and incredible explanations to the court to justify the factual misrepresentations contained in the TRO application. Their duty to investigate began when Mr. Lambe discovered the three mistaken seeds. The duty became even greater when the court ordered them to defend themselves against Rule 11 sanctions.

Several times during the July 5, 1987 hearing, Finley, Kumble attempted to persuade the court that it had conducted a full investigation in preparation for the December and January Rule 11 hearings. In light of the ultimate explanations offered to this court for the inaccurate information contained in the TRO, however, I find their investigation was unreasonably inadequate. In determining whether a party or attorney should be sanctioned pursuant to Rule 11, the standard used is an objective one of

reasonableness under the circumstances, rather than a subjective one. *Rodgers v. Lincoln Towing*, 771 F.2d 194, 205 (7th Cir. 1985); *Eavenson v. Holtzman, et al.*, 775 F.2d 535, 540 (3rd Cir. 1985). Sanctions are appropriate when brought against an attorney, who, after a reasonable inquiry, knew or *should have known* the argument was unwarranted. *Smith v. United Tr. Union*, 594 F. Supp. 96, 101 (S.D. Cal. 1985) (emphasis added). When it appears that a competent attorney, after reasonable inquiry, could not have formed a reasonable belief that the pleadings were well-grounded in fact, sanctions shall be imposed against that attorney. *Eastway v. City of New York*, 762 F.2d 243, 254 (2d Cir 1985).

In the factual portion of this recommendation, I more thoroughly described the inherent incredulity of two of the proffered explanations. I find a reasonable and competent attorney, indeed a reasonable person, should have known the arguments presented to this court at the December and January hearings were not only unreasonable, but incredible and untenable. A competent attorney could not have formed a reasonable belief, after reasonable inquiry, that the explanations contained in those pleadings and professed at those hearings were well-grounded in fact. When presented with the April 3, 1987 Report and Recommendation, recommending sanctions, Business Guides and Finley, Kumble hired new and separate counsel and apparently finally decided to take this matter seriously.

Business Guides' new counsel, Heller, Ehrman, White & McAuliffe ("Heller, Ehrman"), had less time to conduct an inquiry than did Finley, Kumble, but was able to uncover the new evidence albeit assuredly not without much investigation. Mr. Bomse of the Heller, Ehrman firm explained it took counsel "hundreds of hours" to come up with the ultimate explanation. (RT 7/5/87 p. 122.) The point is, however, Heller, Ehrman, as we suggest would be the response of any reasonable attorney, was not satisfied with the explanations offered to this court due to the incredible coincidences that must be accepted to adopt these explanations. In Mr. Bomse's closing argument at the last hearing he stated: "I don't think that there's anything magical about Heller, Ehrman, let alone about Steve Bomse in this. I think that once any lawyers start asking that question, which is what your

report said, 'How could there be a coincidence? How could there be Bledsoe rather than Blodsoe? How could there be 3845 rather than 3545?', it's not a revelation at all. It is just something that, when you sat down and put into the matter the kind of time we, of necessity, did, because your Honor's charges were not only perfectly understandable, they were very serious. But when you get that kind of a situation, you do what we do: you come up with what I think is quite clearly the explantation." (RT 7/5/87 p. 126-127.) Mr. Bomse goes on to argue that plaintiff and Finley, Kumble should not be faulted for not coming up with the explanation, assumably because they were not in the position to have my conclusions in front of them at the time they were preparing their defense. With this argument, I disagree. The parties had before them these explanations; indeed, *they* presented them. No reasonable person would have been satisfied with these explanations. Discerning the incredible coincidences prevalent in these explanations was no great intellectual feat. Finley, Kumble and Business Guides did not need this court to point out the blatant errors in the logic of their representations. They should have discovered the errors themselves; and not being satisfied with these representations, should have done what Mr. Bomse "of necessity" did: spent the hours needed to find the correct explanation. Mr. Bomse notes finding the correct explanation was necessary because of the seriousness of my recommendations. I believe Heller, Ehrman is selling itself short. I am confident that with the competence this firm has shown, no such seriousness of findings would have been needed to prompt such an investigation. I suggest the "mere" request to defend oneself in a Rule 11 hearing would have been serious enough to prompt a thorough investigation by Heller, Ehrman, as well as any other competent and reasonable attorney. It should not take the threatened imposition of sanctions or discipline and contempt proceedings to bring attorneys to fulfill their duties as officers of the court.

It is noteworthy that Ms. Burdick realized the inherent incredulity of plaintiff's explanations. At the July 5 hearing, when referring to the "Bledsoe/Blodsoe" seed, she stated: "Of course you couldn't choose to change one letter . . . . how could you just choose to change just the 'E' to the 'O' and the 'O' to the 'E' and

make that conscious choice and have it come out to be the truth, that kind of coincidence. No, that couldn't have happened. I understand now . . . why that was a problem." (RT 7/5/87 p. 93.) I suggest plaintiff and Finley, Kumble should have understood THEN, at the time of the offering of these incredible explanations, "why that was a problem." I suggest if any one of them had taken the time to simply *evaluate* their arguments, let alone conduct a more thorough investigation, the incredulity of their explanations would have become plainly apparent. They then would have "of necessity" conducted a further investigation. It is for their failure to do both of these that I recommend Rule 11 sanctions be imposed.

Mr. Lambe testified Business Guides relied on Finley, Kumble to determine what evidence they were going to present and what facts they would bring to the court's attention because "[t]hey're [the] professionals." (RT 7/5/87 p. 41-42, 49.) I find there is some force to Lambe's testimony. I believe Finley, Kumble and Business Guides, however, are in the best position to determine who is responsible for the sanctionable activity. A court has the authority to sanction a party jointly and severally because the parties are in the best position to determine who caused the activity to be taken. *Bricklayers v. Martin Jaska, Inc.*, 752 F.2d 1401 (9th Cir. 1985). I therefore recommend sanctions be brought against both plaintiff and Finley, Kumble, jointly and severally.

Many would suggest Mr. Ephraim Margolin, the attorney who represented these parties at the December and January hearings wherein these incredible explanations were first offered should also be sanctioned for taking part in the presentation of such incredible arguments and for himself failing to conduct an appropriate inquiry. "[I]f the duty imposed by [Rule 11] is violated, the court should have the discretion to impose sanctions on either the attorney, the party the signing attorney represents, or both . . . , and the new rule so provides." Fed. R. Civ. Pro. 11, advisory committee's note. "Rule 11 directs that the sanctions should fall upon the individual responsible for the filing of the offending document. In a given case, this could be the attorney, the client, or both." *Chevron U.S.A. v. Hand*, 763 F.2d 1184, 1187 (9th Cir.

1985). Although I think a reasonable person would have recognized the inherent incredulity of the proffered explanations, I believe evidence exists which supports my assumption that Mr. Margolin was not the individual responsible for filing the briefs containing the offending explanations.

There are many citations from the transcript of the July 5 hearing indicating it was Finley, Kumble, not Mr. Margolin, that was intimately involved with the defense of both Business Guides and Finley, Kumble in the Rule 11 action. Upon questioning by the court at the last hearing, Mr. Gelb, a partner at Finley, Kumble, stated he was involved in preparation of the Finley, Kumble attorneys for the December hearing. (RT 7/5/87 p. 58.) He stated that as a member with responsibility for the firm's ethics and practices around the nation, Rule 11 matters come to his attention. (*Id.*) He noted that when Judge Conti initially denied the TRO and it was indicated the matter would be sent to me for further proceedings, his role in this matter began. In January 1987, following the December hearing which involved only Finley, Kumble, and in preparation for the January hearing which was to include only Business Guides, there were a number of conferences in the Finley, Kumble New York offices. (RT 7/5/87 p. 23.) There is no mention of Mr. Margolin even being present at these meetings. He was, after all, the counsel of record; one would assume he would be present at such a meeting held to prepare for the hearing. There is much reference, however, to the presence of two Finley, Kumble partners, Mr. Bamberger and Mr. Gelb. Mr. Gelb explained his role in this case was (1) to conduct an inquiry on behalf of the firm to determine what their performance had been and whether or not it met proper standards; and (2) to ensure the client was protected because a potential conflict of interest existed between the firm and its client. (RT 7/5/87 p. 58-59.) Gelb explained he began to assist Mr. Margolin in his preparation as counsel once it was understood Margolin was to conduct the hearings.

Gelb discussed his extensive conversations with Ms. Burdick and how he felt she would make a "terrific witness." (RT 7/5/87 p. 65-67.) Burdick testified that "many times when [she and Gelb] spoke, [she] brought down [to his office] the parade of

books, everything, the notes, the questionnaires, the papers, the affidavits . . . " (RT 7/5/87 p. 116.) Burdick testified she flew out and met Mr. Margolin *the day before* the hearing. Their meeting was only "a strategy meeting, you know, what was going to be asked . . . how to prepare a situation." (*Id.* at 118.) She acknowledged that the investigations into the matters occurred during her meetings with Finley, Kumble. (*Id.*)

Finley, Kumble is a very large law firm with a great deal of support staff. In this case, the litigation department itself was directly involved. It had personal interests to consider: the defense and therefore possible preservation of an old and profitable client, in addition to its own defense from Rule 11 sanctions. I conclude from all the facts presented, that despite his role as defense counsel at the December and January Rule 11 hearings, Mr. Margolin was not responsible either for the failure to present the correct information or for the presentation of the wholly unreasonable explanations. I therefore do not believe Mr. Margolin should be included in this proceeding.

DATED: September 14, 1987

Respectfully submitted,

FREDERICK J. WOELFLEN,
Chief, United States Magistrate

ENDNOTES

1. It should be emphasized that plaintiff's retraction came only after the court made more specific inquiries.

2. The seed that could not be confirmed at these earlier hearings was later sufficiently confirmed at the July 5, 1987 hearing. The court is now satisfied that this seed was valid and plaintiff's representations regarding it were correct.

3. Note this list does not include the three seeds plaintiff retracted upon the court's requests for further information.

NO. ~~C-86-6164~~ SC (FW)

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

BUSINESS GUIDES, INC.,
Plaintiff,

vs.

CHROMATIC COMMUNICATIONS ENTERPRISES, INC.
and MICHAEL SHIPP,
Defendants.

MAGISTRATE'S REPORT AND RECOMMENDATION

1. BACKGROUND

In the underlying action, plaintiff Business Guides is seeking an injunction and damages for copyright infringement involving the alleged improper copying of one of its business directories. Defendant Chromatic Communications has denied infringement and asserts it used only independent sources in preparing its directory.

Plaintiff applied for a temporary restraining order ("TRO") and submitted affidavits under seal and *in camera* alleging that if the information contained in the affidavits was disclosed to the public, the effectiveness of the devices used to apprehend copyright violators would be lost. The trial judge, Honorable Samuel Conti, requested the undersigned magistrate to conduct an evidentiary hearing concerning possible sanctions resulting from plaintiff's misrepresentations to the court in the TRO application. The undersigned has held two evidentiary hearings. The first was ordered to determine whether plaintiff's counsel, Finley, Kumble, Wagner, Heine, Underberg, Manley, Myerson & Casey ("Finley, Kumble"), should be sanctioned pursuant to Rule 11. The second hearing was ordered to determine whether plaintiff itself should be held subject to Rule 11 sanctions.

We recommend sanctioning both plaintiff and its counsel, Finley, Kumble. We believe plaintiff should be sanctioned for both presenting false information to the court in its TRO application and for what we believe to be the subsequent attempt at a

cover-up. Although we do not think Finley, Kumble should be sanctioned for filing the TRO application, we recommend sanctions against the firm for its part in the subsequent defense of both itself and its client from Rule 11 sanctions.

II. STATEMENT OF FACTS

Plaintiff publishes directories for different areas of retail trade. In 1983, plaintiff began publishing an annual computer-related directory. Plaintiff testified that due to its concern that a competitor might pirate its directory, it planted false information, called "seeds," in its directory. Various street addresses and zip codes were altered by one digit, or names were misspelled so that if the same false information was subsequently printed in a competitor's directory, plaintiff would have strong evidence of copyright infringement.

In early October, 1986, a representative of plaintiff contacted Michael Bamberger, a partner in Finley, Kumble's New York office and told him plaintiff believed that defendant, Chromatic, had copied plaintiff's directory and had reformatted it as a diskette. Plaintiff based this belief on the alleged discovery of plaintiff's seeds in defendant's diskette. Plaintiff based this belief on the alleged discovery of plaintiff's seeds in defendant's diskette. Bamberger contacted Finley, Kumble's Beverly Hills office and requested assistance from a partner, Michael Dempsey, and an associate, Lisa Margolis. Finley, Kumble then prepared to TRO to keep defendant from marketing its directory at the upcoming Comdex trade show. Ms. Margolis signed the TRO application. Finley, Kumble prepared affidavits for plaintiff's sales representative, Victoria Burdick, and publisher, Michael Lambe. The affidavits stated defendant had copied plaintiff's seeds. Burdick's affidavit further identified the entries containing the seeds in attached copies of excerpts from both plaintiff's and defendant's directories. Both Burdick and Lambe testified they reviewed, edited, and executed those affidavits. Both affidavits were filed under seal in support of the TRO application.

In the attached copies to Burdick's affidavit, plaintiff indicated only those entries in the directory which contained the seeds.

Plaintiff did not specifically identify what was incorrect about each entry. Robert Funsten, Judge Conti's law clerk, asked Finley, Kumble to be more specified in its identification of the seeded information. He wanted to know what was incorrect in each indentified entry. Lisa Margolis requested this information from plaintiff. She then contacted Mr. Funsten. Ms. Margolis informed Funsten that although plaintiff had asserted in its signed affidavits that defendant copied ten of plaintiff's seeds, plaintiff retracted its claims regarding three of the ten.[1] Margolis then specifically identified the seeded information contained in the remaining seven seeds and provided the alleged "correct" information. For example, she told Mr. Funsten that in one of the entries, COMPUTERLAND, the street adress had been altered. She indicated that the address both plaintiff and defendant had printed in their directories, 3545 Bay Road, was incorrect and had been planted by plaintiff as a seed. She told Funsten the correct address was 3845 Bay Road.

Because the affidavits were made under seal and defendants had no opportunity to respond to plaintiff's allegations, and because of the suspicious retraction of three of the seeds, Funsten called one of the entries which he was told contained seeded information to determine the accuracy of plaintiff's representations. He discovered the alleged incorrect information was actually correct. Funsten proceeded to telephone each of the remaining six seeds. He discovered the information contained in four was entirely correct (i.e., neither plaintiff's nor defendant's directories contained the incorrect information plaintiff said they did). Of the three remaining seeds, one could not be confirmed and the falsehood of another is questionable at best. (See below). Only one is a verifiable true seed (i.e., the falsity of the information given to the court has been confirmed).[2]

We have divided this report into two parts. The first is this court's recommendation concerning sanctions against plaintiff itself. The second is our recommendation concerning Finley, Kumble.

A. SANCTIONS AGAINST PLAINTIFF

Below is the list of seeds which plaintiff alleged defendant copied.[3] Included is the information plaintiff presented to the court as accurate and the information the court has since determined to be accurate.

SEED #1: *Eagle Micro Systems*

Plaintiff represented to the court that in this seed it printed Eagle Micro Systems' zip code incorrectly: 63830. The correct zip code was alleged to be 36850. Plaintiff asserted defendant copied the incorrect zip code, 63830, and this is evidence of infringement.

The court discovered defendant did *not* copy plaintiff's incorrect zip code. Furthermore, the zip code plaintiff represented as correct, 36850, was incorrect. The correct zip code was that listed by defendant in its directory; 36830. In addition, defendant printed an error in the company's address which plaintiff did not. The street name was correctly printed by plaintiff: GAY STREET. Defendant incorrectly printed GRAY STREET.

At the first hearing where only Finley, Kumble was present, the firm offered no explanation for the factual misrepresentation. At the second hearing, when asked to explain the factual discrepancies, Victoria Burdick told the court only that when making the assertions surrounding Eagle Micro Systems, she relied on plaintiff's master list of seeded information.[4]

Burdick's response, however exculpatory it may be of her own personal conduct, in no way abrogates plaintiff's responsibility for offering patently inaccurate information to the court.

Plaintiff was given ample opportunity to explain the misrepresentations. The only explanation offered was Burdick's assertion that she relied on the master list. This is non-responsive. The court can come to no other conclusion but that plaintiff has not explained the misrepresentations because it could not without implicating itself further.

SEED #2: *Computerland*

Plaintiff informed the court that this seed was created by printing Computerland's street address incorrectly: 3545 Bay Road. Plaintiff asserted defendant copied this incorrect information and this is evidence of infringement. The correct address was alleged to be 3845 Bay Road.

Upon further investigation, the court discovered the correct address is indeed 3545 Bay Road, as listed by defendant.

At the first hearing, Finley, Kumble offered no explanation for this misrepresentation. At the second hearing, Ms. Burdick testified the information relied upon when making representations to the court came from the actual questionnaire sent to Computerland, i.e., from Computerland itself.[5]

If we are to believe plaintiff's explanation, we must first be persuaded that Computerland inaccurately completed the questionnaire; Computerland would have had to mistakenly list its address as 3845 Bay Road, instead of 3545 Bay Road. We must further be persuaded that plaintiff created 3545 Bay Road as a seed and it was entirely by coincidence that the seeded address, created by plaintiff, turned out to be the correct address. The court finds such an incredible set of circumstances very difficult to believe.

SEED #3: *Price Electronics Corporation*

Plaintiff represented to the court that this seed was created by planting an entirely incorrect address: 204 West Carpenter Avenue, Wheeling, Illinois, 60090. Plaintiff asserted defendant copied this incorrect address and this is evidence of infringement. The correct address was alleged to be 1813 Elm Dale Avenue, Glenview, Illinois, 60025.

The court discovered the correct address is 204 West Carpenter Avenue, Wheeling, Illinois, 60090, as listed by defendant.

At the first hearing, Finley, Kumble's New York partner, Mr. Bamberger, testified that plaintiff listed the address to which Price Electronics was planning to move *as a seed.* At the second hearing, Ms. Burdick offered the same explanation.

We first note that plaintiff's purpose in using seeds was to have strong evidence that a competitor had copied its directory. Seeded information should involve such things as misspellings, numerical alterations, or anything else unlikely to be found in a competitor's directory. Here, plaintiff asks us to believe that it chose an address to which it knew Price Electronics had already moved or would soon be moving[6], as a seed.

First, it makes no sense for plaintiff to have listed any other address than that address to which it knew Price Electronics had moved or would soon be moving. Second, nothing indicates defendant would be unable to obtain this new or future address from Price Electronics. It would therefore make no sense for plaintiff or defendant to list Price Electronics' former or soon to be former address when the new address was available. We thus doubt the good faith of plaintiff's explanation.

SEED #4: *Computer Discount of America*

Plaintiff asserted this seed was created by printing the company's name incorrectly: COMPUTER DISCOUNT OF AMERICA. The correct name of the company was alleged to be COMPUTER DISCOUNT OF NEW JERSEY. Plaintiff contends defendant's inclusion of the name COMPUTER DISCOUNT OF AMERICA in its directory is evidence of infringement.

Upon further investigation this court was informed this company is now called WORLD OF COMPUTERS, but was formerly called COMPUTER DISCOUNT OF AMERICA, as listed by defendant. Although there was much confusion over this seed at the first hearing, plaintiff's publisher later filed a declaration purporting to explain the misrepresentation. The court also questioned Ms. Burdick about the misrepresentation at the second hearing. Plaintiff asserted that in 1983 this company informed plaintiff its name was COMPUTER DISCOUNT OF AMERICA. In 1984, plaintiff learned that the retail store was not called COMPUTER DISCOUNT OF AMERICA, but COMPUTER DISCOUNT OF NEW JERSEY. Plaintiff alleged it continued to list the company name as COMPUTER DISCOUNT OF AMERICA as a seed.

Plaintiff asserts that after the court's investigation began plaintiff discovered COMPUTER DISCOUNT OF AMERICA was the name of the company's mail order operation. Plaintiff contends the mail order operation changed its name to WORLD OF COMPUTERS and is now and always has been a separate and distinct entity from the retail store, COMPUTER DISCOUNT OF NEW JERSEY.

As plaintiff asserts, the retail store and the mail order operation are separate and distinct entities. It appears that the information defendant was attempting to list was that of the mail order operation, not the retail store. The address and phone number defendant listed below the company's name is that of the mail order branch, not the retail store. (Alternatively, defendant could have mistakenly included the mail order name, address, and phone number for the retail store.) The information plaintiff listed, however, pertained to the retail store. Defendant therefore properly listed COMPUTER DISCOUNT OF AMERICA as the name of the entity it was listing; plaintiff improperly printed it. This court finds no evidence of infringement. Furthermore, we question the good faith of plaintiff's allegations. When preparing the affidavits in support of the TRO, plaintiff should have noticed the address and phone number it listed were different than those listed by defendant. Moreover, after the court questioned plaintiff's representations, surely plaintiff would have then noticed the differences in address. Plaintiff continues to contend, however, that defendant's use of the name COMPUTER DISCOUNT OF AMERICA is evidence of infringement.

SEED #5: *Premier Source of Distributing, Inc.*

Plaintiff asserted this seed was created by spelling the company's sales manager's name incorrectly: BLEDSOE. Plaintiff alleged the true spelling was BLODSOE. Plaintiff asserted defendant's inclusion of the incorrect spelling, BLEDSOE, is evidence of infringement. The court discovered the correct spelling of the sales manager's name is BLEDSOE, as defendant listed.

At the first hearing, Mr. Bamberger testified Premier Source informed plaintiff that the sales manager's name was BLODSOE.[7] Bamberger testified it was only a coincidence that the

information represented to the court as incorrect seeded information (BLEDSOE) was actually correct. At the second hearing, Ms. Burdick offered the same explanation.

At both hearings, plaintiff and Finley, Kumble offered a document in support of their explanation. The document was marked into evidence as Exhibit No. 1-N, a copy of which is attached hereto. The document is purportedly a copy of a questionnaire plaintiff sent to Premier Source which Premier completed and then returned to plaintiff. On side two of the questionnaire, where it asks the name of the sales manager, is printed the name DON BLODSOE.

Although this court is aware that by doubting the veracity of plaintiff's allegations concerning this seed, it necessarily questions the genuineness of the supporting document, we think a plaintiff capable of offering what we perceive as deceptive explanations in support of its defense, not beyond offering a document of questionable legitimacy.

We note that in order for the court to believe defendant's explanation, plaintiff must first persuade us that Bledsoe's company incorrectly spelled his name on the questionnaire. More importantly however plaintiff must persuade us that it was merely coincidental that plaintiff chose to alter, among thousands of listings contained in the directory, first, this particular listing; second, this particular word in the listing; and third, this particular letter in the word, resulting in an alteration which turned out to be the true spelling of this man's name.

We note plaintiff has asked us to believe that another very similar coincidence occurred in seed number two. We find the occurrence of two such similar and incredible coincidences difficult to believe.

SEED #6: *NFR Computer Room*

Both plaintiff and Finley, Kumble represent that this entry is entirely fictitious. They allege no such company exists. Plaintiff contends it invented the name and address as a seed. They assert the inclusion of this totally fictitious company in defendant's directory is evidence of infringement.

Although this may indeed be a totally fictitious company (i.e., an accurate seed), this court cannot verify plaintiff's allegations without involving itself in investigations it believes to be beyond the court's ambit. The other seeds included telephone numbers and were therefore simple to verify. The NFR seed is a New York company with no telephone number listed. Even though at this point we question the veracity of any of plaintiff's representations, the court will not go to extreme lengths to verify the existence or nonexistence of this company. We shall thus give plaintiff the benefit of the doubt and assume its allegations regarding this seed are correct.

SEED #7: *Computers and Applications*

Plaintiff represents it created this seed by incorrectly printing the store manager's name: DAVID CHOY. Plaintiff asserts the correct spelling is CHOI. Plaintiff contends inclusion of the misspelled CHOY in defendant's directory is evidence of infringement.

The court has discovered the correct spelling of the sales manager's name is indeed CHOI. This is the only instance where plaintiff's representation to the court proved correct.

Rule 11 of the Federal Rules of Civil Procedure provides in pertinent part:

> Every pleading, motion, and other paper of a party represented by an attorney shall be signed by at least one attorney of record in his individual name... A party who is not represented by an attorney shall sign his pleading, motion, or other paper... The signature of an attorney or party constitutes a certificate by him that he has read the pleading, motion, or other paper; that to the best of his knowledge, information, and belief formed after reasonable inquiry it is well grounded in fact and... that it is not interposed for any improper purpose...

We must first address whether Rule 11 applies to a represented party. The text of Rule 11 is silent regarding the duties of a party represented by counsel. In the advisory committee's note, the committee refers to conduct of the "signer." Plaintiff argues that

since it was represented by counsel, plaintiff itself should not be held subject to sanctions. The advisory committee also notes however that "[i]f the duty imposed by the rule is violated, the court should have the discretion to impose sanctions on either the attorney, *the party the signing attorney represents,* or both..., and the new rule so provides." Fed. R. Civ. Pro. 11, advisory committee's note (emphasis added). "Rule 11 directs that the sanctions should fall upon the individual responsible for the filing of the offending document. In a given case this could be the attorney, the client, or both." *Chevron U.S.A. v. Hand,* 763 F.2d 1184, 1187 (9th Cir. 1985).

We think plaintiff should be held responsible for filing this TRO application. Plaintiff provided counsel with these "facts" and alleged such facts to be evidence of defendant's infringement. We therefore recommend holding plaintiff in violation of Rule 11. As laid out more extensively above, we find plaintiff's allegations not "well grounded in fact." We also think its allegations were "interposed for [an] improper purpose."[8]

B. SANCTIONS AGAINST FINLEY, KUMBLE

We believe Finley, Kumble should not be sanctioned for filing the TRO application. The attorney's duty to inquire into the validity of a client's allegations is "one of reasonableness under the circumstances." Fed. R. Civ. P. 11 advisory committee note. "[W]hat constitutes a reasonable inquiry may depend on such factors as how much time for investigation was available to the signer [or] whether he had to rely on a client for information as to the facts underlying the pleading, motion, or other paper..." *Id.*

Here, plaintiff was an old client of Finley, Kumble and had been publishing business directories for many years. Finley, Kumble testified it relied on plaintiff's informaton because plaintiff is a sophisticated business entity which had successfully litigated copyright infringement cases in the past. The firm asserted it believed there was an urgent need for the TRO in order to prevent defendant from competing against plaintiff at the upcoming Comdex trade show. Because of the time pressure, Lisa Margolis testified she worked all weekend preparing the application. Finley,

Kumble requested its client to execute affidavits specifying the basis for its claims and it gave plaintiff the opportunity to review and edit them. We believe the firm undertook a reasonable investigation *under the circumstances*. Considering the longevity of the relationship between the firm and its client, and especially in light of the severe time constraints under which Finley, Kumble found itself, we do not recommend holding the firm subject to Rule 11 sanctions.

This does not end our inquiry however. Although we think sanctions are inappropriate for the conduct surrounding the application for the TRO, we question the firm's actions in defense against those sanctions.

Finley, Kumble alluded that once it discovered the court planned to hold an evidentiary hearing regarding the appropriateness of sanctions for the misrepresentations found in the TRO application, it conducted an investigation. Assumably, Finley, Kumble requested explanations from its client.[9] When questioned at the hearing, Finley, Kumble offered the court the same explanations as did plaintiff. If Mr. Bamberger had taken the stand and said simply we relied on our client and this is what it told us, this court would not recommend sanctions. Bamberger, however, took the stand and presented those explanations as his own. As previously noted we find such explanations entirely untenable. We further find it impossible to believe Finley, Kumble truly believed such remarkable facts and coincidences. We think Finley, Kumble attempted to protect an old and profitable client. Lying on the stand, under the penalty of perjury, carries advocacy too far. We suggest this sort of misrepresentation is of a most serious kind. We therefore recommend disciplining these attorneys pursuant to Local Rule 110-7.[10]

> "In the event any attorney practicing before the court engages in conduct which may warrant discipline or other sanctions, the court or any judge may initiate proceedings for contempt under Title 18 of the United States Code and Rule 42, Federal Rules of Criminal Procedure, or may, after reasonable notice and an opportunity to show cause to the contrary, take any other appropriate disciplinary action against the attorney. In addition to the foregoing, the court or

> any judge may refer the matter to the disciplinary body of any court before which the attorney has been admitted to practice."

DATED: April 3, 1987

Respectfully submitted,

FRANK WOELFLEN

Frank Woelflen, Chief
United States Magistrate

ENDNOTES

[1]It should be noted that plaintiff's retraction came only after the court made more specific inquiries.

[2]In addition, one of the "seeds" that actually contained correct information contained an independent error in defendant's director. Defendant erred in spelling the street name; plaintiff did not. This suggests defendant did *not* copy plaintiff's directory.

[3]Note this list does not include the three seeds plaintiff retracted upon the court's request for further information. Note also that none of this information was provided to the court until the court requested further specificity.

[4]The master list of seeds was apparently prepared by gathering altered information taken from questionnaires, together with the "correct" information, and placing the information side by side on one piece of paper.

[5]She testified however that she was unable to produce this questionnaire because plaintiff saves hundreds of thousands of questionnaires and retrieval of a specific questionnaire can take months.

[6]At the second hearing, Ms. Burdick testified that Price Electronics' address changed in 1985. The directories at issue are for the years 1985 and 1986.

[7]This court acknowledges this testimony amounts to hearsay evidence but due to the uniqueness and lack of formality of the hearing, we chose to allow the testimony to lend whatever weight we believed appropriate.

[8]The validity of two of plaintiff's seed is irrelevant to this action. We believe the intentional misrepresentation to the court of even one seed is sufficient to warrant these sanctions.

[9]We have not entirely dismissed the idea that Finley, Kumble may have been aware of the misrepresentations in support of the TRO application from the beginning. We have no evidence supporting this proposition, however, and therefore assume the firm was not in collusion with its client at this time.

[10]Although we can make no specific recommendations as to which attorneys within the Finley, Kumble firm should be sanctioned, we do believe Lisa Margolis, although intimately involved in the application for the TRO, was sufficiently removed from the defense of this action. Therefore, except as in regard to her affiliation with the firm, we recommend no sanctions be personally levied against her.

DISTRICT OF CALIFORNIA

C 86 6164 SC

Exhibit No. 1-N

Date Entered: ____________

WILLIAM L. WHITTAKER, Clerk

By: ________________________

Deputy Clerk

Dear Computer and Software Distributor:

We are updating our database of computer and software distributors from which our directory of "Computer & Software Distributors" is derived. Our research has identified you as a computer and software distributor not presently on our file. To be included — free of charge — please answer the questions below and return this form to us in the enclosed post-paid return envelope.

This questionnaire should be answered by company headquarters only; if we inadvertently mailed to a branch office — please forward this to your headquarter.

Please enclose a list of your accounts, if available.

Thank you for helping us complete the most authoritative and comprehensive database of computer and software distributors in the U.S.

Cordially,

Michael Lambe
Executive Editor

1. Company Name: Premier Source Dist. Inc.
2. Headquarter Address: 1882 McGaw, Irvine, CA 92714
3. Headquarter Telephone: (714) 261-2011
4. What Product Lines do you distribute?
   ☒ Computers (581) PLEASE LIST ALL BRAND NAMES AND MODEL NUMBERS/NAMES
   Zenith-Models Z-100, 150, 160, 2T01, 05, 06
   Televideo-Models TS-802, 803, 802H, 806, 816, 806H, 1603, 1600 series, 1605, TV01, 03, 04, 07, 08, 10, 11, 12, & 13

   ☒ Software: ☒ Systems (591) ☐ Video (594)
   ☐ Personal (592) ☐ Educational (596)
   ☐ Entertainment (593) ☒ Business/Professional (595)

   ☒ Other: ☒ Monitors (582) ☐ Accessories (588)
   ☒ Storage Devices (583) ☐ Supplies (589)
   ☒ Printers (584) ☐ Books/Magazines (760)
   ☒ Modems (585)
5. Do you operate retail locations as well as distribute? ☐ Yes. ☒ No. If yes, what % retail? ______
   And how many stores do you operate? ______
   Where are they located? (city, state) ______________
6. Do you manufacture as well as distribute? ☐ Yes. ☒ No.
   If yes, what % manufacturing ______________
7. Who do you distribute to:
   ☒ Computer Stores ☒ Systems Houses
   ☒ Mass Merchandisers (Department Stores, Discount Stores, etc.) ☒ Office Supply/Equipment Dealers
   ☐ End-Users ☐ Consumer Electronics Stores
   ☐ Other Distributors ☐ Other (Please Specify) ________
8. In what states do you have accounts? ______________
9. How many full time sales people do you employ? 10
10. How many trucks do you operate? 2

11. What is the total square footage of your warehouse(s)? 24,000

12. Do you operate any subsidiaries, divisions and/or branches (other than sales offices)? ☒ Yes. ☐ No.

Street Address	City	State	Zip	Manager
4455 E. Camelback	Phoenix	AZ	85018	
8388 Vickers	San Diego	Calif.	92111	

13. Is your company a subsidiary or division of another company? ☐ Yes. ☒ No. If yes, who is your parent company? ________
Hdq. location? ________
If no, ☐ public or ☐ private company.

14. In what year was your company founded? 1980

15. What percentage of your annual sales are in the following areas?

Distribution	100 %
Retail Store Sales	%
End-User Sales	%
Manufacturing	%
Other Operations please specify: ___	%
Total	100%

16. Key Personnel:
Owner: Tom Dodge
President: Tom Dodge
VP: ________
Marketing Mgr.: ________
Advertising Mgr.: ________
Sales Mgr.: Don Blodsoe
Technical Mgr.: ________
Customer Support Mgr.: ________
Hardware Mgr.: ________
Software Mgr.: ________
Buyer: ________
Buyer: ________
Other: Don Coley — General Manager

17. What was your annual sales for last full year? $________
And how is it broken out by category in percent?

Computers	%
Peripherals	%
Software	%
Accessories/Supplies	%
Books/Magazines	%
Other please specify:	%
Total	100%

Information provided by: ________
Date: ________

Please return filled-in form to:

CHAIN STORE GUIDE,
425 Park Ave.,
New York, N.Y. 10022.

Thank you.